ANTI-CORRUPTION COUNCIL
OF THE GOVERNMENTOF THE REPUBLIC OF SERBIA

CORRUPTION, POWER, STATE

PART III

Editor
Verica Barać

Belgrade
2011

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OF THE REPUBLIC OF SERBIA

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FOREWORD

This is the third book issued by the Anti-Corruption Council of the Government of the Republic of Serbia, published at the end of the tenth jubilee anniversary of the Council's operation. Like the previous two books, *Corruption, Power, State III* does not include all the activities of the Anti-Corruption Council, but rather a selection of key analyses and recommendations made by the Council from 2007 to 2011.

Part I of the book includes the most significant papers presented at the *Belgrade Transparency Days 2007* conference, organized by the Council in cooperation with the Swiss Embassy in Belgrade and the Basel Institute on Governance, which secured the participation of the most eminent European experts in transparency of public finance. The aim of the conference was to point out the importance of an independent state audit institution.

The Law on the State Audit Institution was adopted on 14 November 2005, and its application was to begin within a period of six months from its adoption. However, by March 2007, when the Council organized the *Belgrade Transparency Days 2007*, the State Audit Institution had not started its work. That is why the Council organized this conference, where it was pointed out how an independent state audit institution is important for fighting corruption. The papers of the foreign and domestic experts presented at this conference are still topical today, as the State Audit Institution still does not perform its basic function.

We also want to take this opportunity to express our special gratitude to his excellence, Swiss ambassador Mr. Wilhelm Meier as, if it had not been for his effort and travail, the *Belgrade Transparency Days 2007* conference would not have been held at all. The conference was the result of continuous help provided to the Anti-Corruption Council by the Swiss Embassy and Mr. Meier, and their help in the creation of the environment for the establishment and work of anti-corruption institutions in Serbia. A year before, in 2006, the Anti-Corruption Coun-

cil and the Swiss Embassy, also in cooperation with the Basel Institute on Governance, had organized the international conference, *Belgrade Anti-Corruption Days*.

Part II of the book includes several of the most significant reports in which, after months-long comprehensive research, the Council revealed drastic phenomena of the systemic corruption in Serbia. These are the reports on the *Horgosh – Pozega* highway concession, *C-Market* privatization, *Luka Beograd* ownership concentration, *Novosti* privatization, pressures on and control of the media in Serbia, the sale of *Delta Maxi*, and the analyses of the Law on Protection of Competition and the Regulation on the Criteria and Procedure for Calculation of Compensation for Conversion of the Rights for Persons Entitled to the Conversion against Compensation.

The steps that must be taken in order to establish an independent state audit institution, which have not yet been taken even six years after the adoption of the Law on the State Audit Institution, together with the analysis of the phenomena of the systemic corruption and its serious negative consequences, provide an answer to the question why and to what extent Serbia is still, in this year, 2011, engulfed in corruption.

In order that the problem of corruption in Serbia be presented vividly, Predrag Koraksic Corax has, in his own distinctive and masterful way, illustrated the book, and we sincerely thank him for that.

Verica Barac
Anti-Corruption Council
President

Република Србија
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CONCLUSIONS AND RECOMMENDATIONS FROM THE CONFERENCE BELGRADE TRANSPARENCY DAYS 2007

Serbia is one of the few countries in the world still without the external state audit of the public finances. The Law on the State Audit Institution was adopted on November 14, 2005. In accordance with the Law the Institution should have been established within six months from the date of its entering into effect. The Law on the State Audit Institution, however, has not yet been implemented. Due to such circumstances, the Anti-Corruption Council in cooperation with the Swiss Embassy in Belgrade, and the Basel Institute on Governance organized a Conference Belgrade Transparency Days on March 6 and 7, 2007, discussing the issues of the budget transparency and the state audit.

The Supreme Audit Institutions are designed to enable the transparency and the integrity of the reports on public finances, representing a crucial link in the chain of institutions destined to create conditions for curbing corruption in the public finances. Two-day's Conference Belgrade Transparency Days 2007, tried to consolidate the principles for the establishment of the efficient and sustainable State Audit Institution in Serbia.

Conclusions

The potential impact of the State Audit Institution on the fight against corruption is manifold:

- The chief task of the State Audit Institution (SAI) is to raise the transparency level as well as the integrity of the reports on public finances, which represents a key element of anticorruption initiatives, above all in the field of prevention of corruption and detection of the corruptive mechanisms;
- The professional quality of the SAI could enhance the professional level of other public institutions;
- If SAI is to be established in a corruption free fashion, and governed by laws and the Constitution of the Republic of Serbia, it may, in that sense, serve as an example for other state establishments;
- The results of the SAI's work may offer a significant backup for the judiciary and the National Assembly in control of the work of the executive power;
- Creating conditions for the transparency of public institutions, being one of the most important SAI's tasks should strengthen the role of the public in the control of the authorities and the fight against corruption. The participants of the Conference stand unanimous that the public, through free media, represents an important factor in the fight against corruption, and that the work of the SAI could offer a significant help to media in control of the public funds squandering. Also, we agree that the political will of the citizens (and not of the political parties on power!) represents a measure of the control of the authorities and the fight against corruption in the society and the state. We believe, therefore, that the work of the SAI in the field of the more transparent expenditure of public funds is to contribute the citizens of Serbia to express their will to live in a democratic state with strong and accountable institutions, which represents the most efficient framework for the fight against corruption.

Recommentations for the Establishment of the State Audit and Enchancement of the Budget Transperency in Serbia

1. **The independence of the State Audit Institution** represents the chief principle of its work as follows:

– *Legal independence*

Legal grounds for the SAI's independence include not only the proclamation of its independence in the Law on the State Audit Insti-

tution, but also amendment to the pitfalls and shortcomings in the Law on the Budgetary System and the Law on Accounting and Audit, as well as the adoption of the necessary by-laws which would govern the field of audit in Serbia more clearly, thus enabling the SAI to operate on the basis of transparent and faithful principles.

The regulations and the principles of accounting and audit in Serbia are not precise enough, and are rather backward in comparison with the practice of the more developed market economies. Also, there are no capacities for their implementation (for example the Law failed to envisage the existence of the Certified Accountant, the criteria for the awarding of professional titles are not precise, translation of the international standards whose implementation is prescribed by the Law is not easy accessible, i.e. a timely translation of the current changes of these standards is not available, etc.)

– *Management independence*

The National Assembly should elect reputable individuals into SAI, people of personal and professional integrity, instead of delegating representatives of the parliamentary parties. This is of key importance for the assurance of the effectiveness of the work of the Institution. We deem, moreover, that the fashion the members of the Anti-Corruption Council have been elected may serve as a raw model for the election of the members of the Council of the SAI.

– *Operative independence*

The Law contains pitfalls and shortcomings concerning the issue of the competent human resource and logistics backup indispensable for the work of the SAI. These pitfalls need to be rectified in order to give SAI the full operative independence.

– *Independence in access to information*

SAI must have an unobstructed access to the information regarding public finances. On February 13, 2007, during the preparations for the Belgrade Transparency Days 2007, the Anti-Corruption Council requested the following reports from the Ministry of Finance: Budgetary Inspection Reports for 2004–2006, as well as the Reports on the Performance of the Budget, the Payment System Internal Control Reports, and the Plans for the Sale of the Republic Non-Financial and Fixed Assets for the same period. According to the Law all documents must be available to the public. However, we did no receive any of the requested documents till the beginning of the Conference. The Cabinet of the Ministry of Finance have said that the

Budgetary Inspection Reports contain delicate information not to be disclosed in public, and the Treasure Department have informed us that they „have no obligation of external informing" when asked for the Payment System Internal Control Reports. Taking into account such an alarming state of the access to important information on the expenditure of the budgetary funds in Serbia, the State Audit Institution stands no chance to fulfil its mandate.

– *Financial independence*

Each of the specified aspects of the independence is of equal importance. If they fail to be established, the SAI's independence although guaranteed by the Law shall not be achieved. Still, financial independence is the most important factor for the independent work of the State Audit Institution. Moreover, financing the work of SAI represents the easiest way to influence its independence.

2. **SAI's Cooperation with other Ministries**, first of all with the Ministry of Finance has to be firmly established, i.e. the situation should be such that the Government acts in accordance with the findings of the State Audit Institution.

3. **The connection with the National Assembly and its Committees** has to be strengthen in each and every aspect, both formally and practically, bearing in mind that one of the chief tasks of the SAI is to assist the National Assembly in performing the most comprehensive control of the work of the executive authorities concerning the public finances.

4. **The implementation of the best international practices and standards**; the experience of the INTOSAI, the Global Association of the State Audit Institutions, could be of importance for the work of SAI, particularly in the beginning, until it learns from its own experience. We deem, nevertheless, that the INTOSAI standards should be incorporated into the SAI's Regulations.

5. **The National Assembly should appoint the Council of the State Audit Institution as soon as possible**. Afterwards, the SAI should start working in the shortest time possible. Subsequent to the establishment of the SAI's Council, its members should:

- Start with the implementation of the Law on the State Audit Institution in practice;
- Define the contracting conditions for private auditors in charge of the state budget audit in the near future, including the years not covered by the audit arrangements;

- Elaborate a Draft of a Strategic Document and prepare preliminary documentation on polices in fundamental operative activities;
- Prepare the necessary Regulations and other additional legal acts;
- Define the Action Plan that would comprise the already specified actions, including the deadlines and the operative schedule.

Taking into account the pitfalls, which no doubt need to be rectified, the Law on the State Audit Institution and the Law on the Budgetary System represent a sufficient legal framework for the establishment of the thrustworthy system of the state audit. We deem, therefore, that the State Audit Institution can and must start working soon, pursuant to the existing laws. Also, that in the next year it has to elaborate trustworthy reports, because that is the only way to win the public trust, both for its own work, as well as for the entire process of the modernization of the public finances.

6. **The State Audit Institution has to fit in the broader context of the modernization of the public finances in Serbia**; i.e. it must not remain detached from the process of reforms of the entire budgetary system.

7. Besides the State Audit Institution, **the enhancement of the transparency of the expenditure of the public funds in Serbia would also benefit from the improved efficiency in penalizing corruption criminal actions in the public sector**. It would also benefit from the enhancement of the work of the investigation institutions and independence of the judiciary, for the experiences of the Western European countries point out that penalizing specific criminal actions (for instance abuse of power in public procurement) had a very important impact on curbing corruption in the public sector.

8. Transparency of the budget in Serbia has been seriously damaged by the National Investment Plan. **It is, therefore, necessary that the Government annuls the NIP and suggests amendments to the Law on Budgetary System, namely to the provisions which, at this moment, enable the breach of the budgetary system in a way the NIP has been doing so far** (prolonged financing of the projects initiated in one year in the next year, and with the funds from the last year's budget; also, continued financing of the projects partially initiated in one year, with the funds from the budget for the next year). In order to have the State Audit Institution operate properly, first of all the Institu-

tion must be familiar with the exact amount of the budget for one fiscal year. The existence of the National Investment Plan as such, financed from the successive budget, would invalidate the work of the State Audit Institution from the start. The State Audit Institution must have a precisely defined and time-limited subject of investigation.

Belgrade,
March 12, 2007

President of the
Anti-Corruption Council
Verica Barać

BELGRADE TRANSPARENCY DAYS 2007
LECTURES

PhD *Yvan LENGWILER*,
University of Basel

THE POLITICAL ECONOMY OF CONTROLLING CORRUPTION

Corruption – always and everywhere

The topic of our conference here today and tomorrow is a dark one. Corruption is an evergreen. It has been practiced probably since the very emergence of human civilization. It is something that happens everywhere. There is no society on Earth that is free of corruption, though the amount certainly differs by a large margin in different places or institutions.

Even though corruption is such a widespread form of behavior, it is generally despised. Corrupt public servants are considered to be parasites who misuse their position of trust for personal benefit in a villainous fashion. And yet, despite the stigma that it carries, it is a widespread phenomenon. Cases of corruption have been detected in all spheres of public activity, such as procurement, judiciary processes, provision of licenses or permits (especially for construction), and others. It also involves semi-public spheres, for instance, political party finance, or the sport industry, such as the recent scandals in the Italian and German football industries. In fact, corruption is also common in purely private interactions, where one agent is in a position of trust or power with respect to his employer, and then uses this position for personal benefit in his interaction with other private agents.

The World Bank has estimated the total sum of bribes paid just in the area of public procurement to be around 200 billion dollars per year worldwide.[1]

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[1] D. Kaufmann (2005), „Six Questions on the Cost of Corruption," *The World Bank News*, Washington, DC,

Two types of corruption

First, we need to distinguish two types of corruption that have to be treated quite differently:

- The first kind is bribes that are paid in exchange for permits that are required for legitimate activities.
- The second kind is bribes in exchange for preferential treatment, for instance, to get the contract in a public procurement process even though one is not the best bidder.

This second form of corruption is something else entirely, because it imposes a cost on society as a whole in the sense that it is not the most economical supplier who gets to build the new bridge or airport or whatever is being procured. This form of corruption is really just like stealing from the tax payer and should be repressed as much as possible. One can, however, prevent it to a large extent by a diligent design of the procurement mechanism.

In the following, I will talk only about the first kind of corruption. It is much less clear that this kind of corruption is bad for society as a whole.

Corruption is the solution...

Homer Simpson — the well-known American cartoon character — once said that alcohol was the cause and the solution to all problems of this world. I don't know about that, but corruption certainly does have these two sides to it. It is the solution when one has to deal with an uncooperative bureaucracy, but it may well be the reason why the bureaucracy is uncooperative in the first place.

The incentive to perform corruption emerges whenever one has to deal with an unhelpful, harassing administration. What should you do if the government official keeps harassing you instead of providing the service he out to provide so that you can go about your legitimate business. Of course, you may have the legal right to receive the permit or license or whatever you need, but to actually receive it, you still need the bureaucrat to cooperate. What should you do if also the judicial system won't help you, maybe because it does not function in a reliable way or is much too slow?

As an example, suppose you want to create a new firm. In some countries, this is very simple; in other countries, it is almost impossible.

The team of Hernando de Soto has compiled a list of the steps that are necessary to create a new legal business in Peru. This list is 31 meters long! Well, when faced with a 31 meter hurdle, one might realize that a little Bakshish here and there could simplify matters considerably. Maybe you can shorten the list to maybe 5 meters or so, because bribes are sometimes able to make a corrupt or lethargic administration work in ways not seen before.

So bribes are not only bad. They give you predictability. You can have what you want – a license, a permit, whatever – it just has a price.

Given a dysfunctional state apparatus, corruption is the better of two evils. It is only the second worst, so to speak. The worst is a dysfunctional, uncooperative state that cannot be made to move even with bribes. Bribes make it expensive to start a new business, but if bribes don't even work, it is impossible to start a new business, which is clearly even worse.

... and the cause

Corruption is like many other things: one needs two to tango. One party has to be willing to pay the bribe and one has to be willing to take it. Now both parties receive a benefit from this transaction: the paying side receives the license he needs from the bureaucrat, and the receiving side receives – well – the money. Whenever a mutually beneficial trade like this presents itself, we should expect rational people to perform it.

The first impulse of the economist is that such a mutually beneficial trade cannot be bad. Nobody is forced into anything and both sides make a gain, so why call it bad or even evil?

The problem is this: from the point of view of the individual citizen who faces a Kafkaesque bureaucracy, corruption appears as an elegant and comparatively cheap solution. From the point of view of the corrupt official, the bribe just appears as an additional opportunity to make some money. The source of this extra income is of course the excessive regulation that is formulated in the law, and the fact that the judicial system is unable to help the citizen to claim his right. The extra money that the bureaucrat extracts for himself would quickly vanish in an environment with more straightforward, transparent regulation that could then also be enforced through the judicial system.

This is the reason why bureaucrats have no interest in simpler regulation. Anything that reduces the predictability of an administrative process creates an opportunity to collect bribes for them, because more decisions are left at their discretion.

So we conclude that from an individual point of view, corruption is beneficial in the short run for both directly involved parties. The person who pays the bribe avoids the harassment and receives the permit he needs, and the bureaucrat receives some extra income. And yet, the fact that corruption is possible is the major reason why the bureaucracy makes life difficult for everyone. The quality of public service and of institutions in general is endogenous. Corruption is a symptom of a dysfunctional administration, as well as a major obstacle on a way to a functioning and efficient government apparatus.

Bribes are a form of taxation

Corrupt bureaucrats are really like highwaymen who make legitimate private activities very expensive. They avoid killing their prey altogether, but they do try to extract as much as possible from them. From an economist's point of view, corruption – or bribes – is really just a form of taxation. But because the tax „authority" in this case is very dispersed – every corrupt official who is in a position to extract bribes levies his own little tax – it is a taxation system that leads to excessive taxation. It comes as no surprise that a system with nearly prohibitive taxation does not create much wealth. This is why a functioning, lean state with transparent regulation is better than a corrupt system: it imposes less heavy taxation on the citizens and thus more private initiative will flourish.

What to do?

So if we have a problem with corruption, how should we address it? There are two ways, which I would like to call the incentives strategy and the opportunities strategy. Let me explain.

One can give bureaucrats incentives not to let themselves be bribed, for instance with abrasive punishments for offenders if they are caught. Part of this strategy would also to be lenient towards whistle blowers, in order to catch the offenders. One can also try to give incentives to citizens not to pay the bribes, for instance by punishing

them if they are caught. What is the result of this incentive strategy? Here's an example: suppose the the permits one needs to open a new legal business are many, and the forms one has to fill out are plenty, and the rules are unclear so that they are subject to discretionary interpretation, and yet, bribes are ruled out or made more difficult, the result will simply be to move from the second worst – the corrupt state which does accept bribery – to the very worst – the dysfunctional, non-corrupt state.

A better way, I think, is the opportunities strategy. It is the intransparency of the regulation that gives bureaucrats the possibility to levy their own little tax by asking people for bribes. It is also the fact that the judicial system does not help citizens to claim their legal rights vis-à-vis the bureaucracy. An ombudsman can go a long way towards making the administration less of a pest. More fundamentally, by making regulation light, easy to understand, not subject to discretionary interpretations, in short, by making the outcome predictable, one robs the bureaucrat of his leverage to raise bribes. This way, one can move from the second best – a dysfunctional but corrupt state – to the first best – a transparent and simple set of rules that regulate private activity in a sensible and predictable fashion.

In practice, one will probably need some of both strategies, but I believe that the focus should be on the opportunities strategy rather than the incentives strategy.

In this process, one might have to pay bureaucrats better salaries than before, to make up for the lost bribes, but the overall effect is clearly positive, because the effective level of taxation is significantly reduced and predictability of the administrative process is enhanced. This allows people to actually plan and perform an economic activity, make innovative ideas become a reality, and will thus help to make society as a whole prosperous and free.

Ian HAWKESWORTH,
Administrator, Budgeting and Public Expenditure Division, OECD

TRANSPARENCY OF BUDGET AS BASIC CONDITION

Let me first take this opportunity to thank you for inviting me here to this very exciting conference. I have already learned a lot about Serbia and it is going to be even more interesting. We at the OECD are very happy to be invited to this. I am going to speak about best practices for budget transparency and this is based on OECD countries` experiences and perhaps I can say that I am talking about opening of the hood of a car, if you will, so that you can look into the machine and see how did in the past work and have the mechanic stand next to you and you can also ask him to say how we are doing and he should ask you truthfully and there is even a manual within so hopefully transparency will make you enable to decide whether or not are these car worth buying.

Basically, my presentation will form three points. I'll discuss what obstacles to strategy of transparency there are. I'll discuss the actual budget principles and then I will discuss some key issues, some issues that are very important and quite difficult to manage.

Now what are the obstacles? I think that many of you in this room know this very well so I will not spend much time on it. Basically there are best interests in all countries. Knowledge is power and some of the knowledge that is contained in the budget is politically sensitive so certain institutions and people might have incentive not to be completely forthcoming with it. Second, it is difficult to communicate. It is very technical. It takes people years to actually understand how the budget works and how the budget process works even if they are electro engineers. So it is just difficult. It is also difficult perhaps for the individuals to see how these issues personally effect them and if it is difficult for the individuals to see, the voters to see how effects them, it is even more difficult to get parliamentarians to be passionate about them. Therefore, Parliament perhaps do not scrutinize as much as would be ideal. This of course is also a product of how technical it is and the lack of capacity to which we will return in a second.

Now the Best Practice on Budget Transparency was agreed in 2001 by directors of OECD countries. These are thirty countries and the budget directors from the OECD meet at least once in year in Paris to discuss topics that are relevant for them. And they asked us at the secretariat to write down honest knowledge into some pretty basic explainable principles which should be in your pack as far as I understand. So it is based on the experience and it supposes to be practical. There are no equations or stuff like that. There are three pillars and the best practices. There are certain reports that should be made. One should not focus so much on the actual report since that just the information should be distributed at certain intervals and should be contained certain information. There are certain disclosures that should be part of transparent process, that's the second thing and the third thing that there should be some processes in place to ensure transparency.

I understand that most of you, if not all of you here, know this process so I am not going to spend time on it. This is attempt to show you the cycle from preparation which takes in its center usually a Minister of finance discussing with the Prime Minister and the Line Ministry about the Budget. It is sent to Parliament who approves it. It is implemented by the executive, by the Line Ministry to the citizens and hopefully it is then audited by Supreme Audit Institution. Now this is just the representation of to say that there is the relationship between these actors and the diffusion of knowledge amongst these that is key to what we are discussing.

These are the budget reports. I am just going to go through them. It looks like a lot of reports but much of the information should not be new to the actors in the cycle. First, let`s have few words about the budget. It is important that is comprehensive. It should cover all expenditures and all revenue. That means we are against ear-marking special funds and so on because it does not allow prioritization to take place openly and in a public debate. Of course there are well functioning countries that have these funds. Those security funds and so on. So one size does not fit all but the key here is that comprehensiveness should be comprehensive and clear. It should also contain some commentary not just the bare figures but just actually Ministry of Finance should be made to explain what is actually in here with words and even better with some kind of performance information. How many students have passed their exams? How many health checks have the food authority performed? It should contain some kind of medium term perspective. That means the budget year and two more years or

three. So that when parliamentarians and others look at the budget they can see which way things are going all other things been equal. Of course, you only pass the law for one year but it gives much greater usage to the document. As I said before, it is important that the budget is presented in gross terms. By this I mean that earmarked, used fees and other kind of activities should be clearly accounted for and be a part of the budget again so we can see what is going on. Assets and liability should be included and discussed – this was also touched upon by previous speakers – and it should be organized in an intuitive way that means administrative unit, economic and functional class. That is the budget. But before the budget there should be the pre-budget report where the government clearly states what is its fiscal policy what is it try to attain and on what bases does it makes economic assumptions about why this budget is the right thing for the country.

It should clearly state what just future look like economically and what are the assumptions to get back to that. And there should be a monthly report. No more than one month old. Which basically gives a continual update on progress not very detailed just expenditures or revenues, borrowing and so on. And there should be a Mid-Year report. And this should be quite a comprehensive update on an implementation. It should also discuss a part from expenditures and revenue development. What is going on with our assets and liabilities especially our financial ones? What is our borrowing and how do our investments look. The Year-End report is specifically interesting for us here today because that is the key accountability document. That it has to mirror the budget in the way it is structured so it can be compare to the budget of course. It should be delivered no later than six months from completion of year. It should be comprehensive. It should be discussed. It should be contain discussions of development and it should be of course be audited by the Supreme Audit Institution. In many countries there is also a Pre-Election report. It should correspond to the Mid-Year report and there should be comprehensive update on how we doing also with the macro figures so that elections can have a sound bases for discussion. And there are also many countries where the Pre-Election reports are not made because for the obvious reasons it is a very political document. But there are examples of the Pre-Election report in Holland with the central planning bureau of actual costs. It means they look at each party program and they come with the assessment of how much will this costs and how would that effect government policies, government expenditure. And the planning bureau is independent. Than there should be a Long-Term report every

four or five years to say if we do nothing under certain assumptions how sustainable are we, how does it look in ten or forty years.

I'll get back to the Long-Terms report. These six points are the specific disclosures that have to be made. Financial liability and assets and non-financial assets again discusses clearly that should be some kind of sensitivity analyses saying what would different changes and how would that effect our financial liabilities and specifically. The non-financial assets are also very important. There was a comment about the sale of buildings. Buildings of course should be a part of this disclosure and they should be valued at market prices so the public knows what it owns and what is worth; this includes equipment and so on. There should be also for equipment deep appreciation and it should be stated how it would be appreciated. And for assets that are herited assets that do not make any sense to be valued it should just be listed.

Now for ensuring integrity we need accounting policies, documents should be clearly state what is the policy. It should be used consistently and any changes should of course be explained. You have to have a system of responsibilities basically it means that you need internal financial control and you need some kind of internal audit and of course you need a real End-Year report audited by Supreme Audit Institution. The next point is I guess is also about a culture. You need a culture of publishing everything. You need to make the Ministry of Finance encourage debate and encourage openness. You need a parliament that has sufficient time and sufficient capacity that means money and staff. So that even if you are not an engineer and you have specialist that can explain to you what is actually in this document; so it has a soft side and a hard side. Now I'll turn to the key transparency issues. Actually we are going to go straight to economic assumptions.

Now this is the primary transparency issue because it is so much money if you have unrealistic assumptions. It can fundamentally derail your budget policy. So being objective as possible is the key. So basically it is not very complicated as is complicated to do but the principle is to basically to disclose all key variables – GDP, growth of inflation, employment, unemployment, interest rates, current account. Everything should be disclosed so everybody can reproduce it. And then there should be sensitivity analysis again to make sure to make it explicit what would happened is things change if our assumptions change. How bad will it look? Some countries have developed this even further. They make systematic comparisons between their old forecast and bank forecast private forecast or blue chip forecast. The Canadians don't even make their own economic assumptions about these things.

They just take an average of five or six banks. You could have independent penals like we talk about Dutch central planning bureau. Or you can have a prudency factor saying that there is a tendency to optimism so you should have pessimism by us be on the safe side. Again, all these safeguards are basically because it is such a big thing when you get this wrong. And it is easy if you sit in a Ministry of Finance and you`d like to make some new initiatives. It is very easy to feel pressure to deliver a more optimistic view than it can actually and ethically be defended.

Accrual accounting in budgeting is very trendy if you can use that word in budgeting circles. And it is designed as you know to provide better, clearer information about what is going on in the public sector. However, it is very complex. And it can be abused for number of reasons because of this complexity because you have to make a lot of decisions, judgments about what, when something is an asset, when something is a liability, when is a continuing liability. So what would you do with none-cash items if you have some kind of equipment assets will you be appreciated? Should that appreciation be handled as with cash? So, we would advise to be very careful with using account accruals what is happening is that some countries, Britain, Australia, New Zealand, Denmark to some extent have gone all the way and have some sort of both accrual accounting and accrual budgeting and mosts or the everybody else is very hesitant towards this. So the consensus at this point is that you should have financial statements on accrual basis and of course on a cash basis becasuse you have to have your budget and your accountance in a same way. But you should have financial statements on a accrual basis. And the idea is also that you should have political meshing principles so that when the decision to build a bridge is made you should, the politicians of the day should actually allocate cash.

Tax expenditures are the budgeting equivalent of a free lunch. It does not really exists but it looks like it. Basically it is the estimated cost tax revenue due to preferential treatment. A typical example is a lower VAT (Value added tax) for food. It is difficult to measure and it is even more difficult to get rid of when it is managed, when it is implemented. There is less scrutiny and over time it tends to disappear. That of course makes it a politically attractive because you do not actually subsidize you just do something – you do not collect those taxes. So the first order of course is just to make it explicit and make some kind of figure, some kind of estimate about how much this is costing us. Actually that is a part of a Serbian budget loan as it is right now. It should be integrated with a regular budget process, there should be a decision about this is

a something we want to keep on doing. Perhaps one could assign these tax expenditures to relevant Ministry so they could choose do they want to continue doing this or do they want to spend the money. Or you could even cap it in some way and have some top down, I mean if Ministry of Finance sends some caps for tax expenditures. The next is also something that is quite dangerous and very popular – and these are Public Private Partnerships (PPPs). My Hungarian friend perhaps can tell more about Hungarian experiences but basically we are very skeptical and we advise you to be very careful if and when you use this. If you are going to do it, it requires that there is a real – and that is very important – risk transfer from the public sector to the private sector because the public sector can always borrow cheaper than the private so you have to believe that this private company can actually built this airport or bridge or whatever much more efficient than the public sector can do for it to make any sense. And you have to make sure that there is not some kind of bail out that will eventually happened. Because if this is not the case it is basically a way of moving big expensive, typically infrastructure investments off budget and tying down cash for thirty – forty years. History of course shows us a lot of bail outs and the next slide is an example. It is the small example but I think it shows you how difficult it can be. This is from Scotland. A company approaches the government and local councils and says why you would want that old ferry why don`t you want nice, shining bridge. And the toll will be probably around one pound. It is quite a lot when the bridge opens and it costs four pounds fifty pence. Of course this creates a huge political storm and in the end government has to buy out the consortium that built the bridge which had a very good deal in the end because it cost them twenty million to build, it took thirty three million in toll and it got another twenty seven million for the government to take over the consortium. One of the experiences from Britain who have been very proficient in using this to a worrying degree is that in UK you can not use PPPs for IT projects simply because they are too complex and there are too many scandals and too much wasted money.

The next one is a continuing liability against something that sounds very boring and can costs a lot of money if it goes horribly wrong. Basically its liability is where you do not know if and when you are going to pay money. Guaranteed programs, insurance, legal claims against the government, PPPs without risk transfer. What can you do with these? You can stop making them of course but if you have them you should try to quantify them and if not possible at least disclose them and have a serious discussion of what they are and what the

chances are they might come to pay. In future one might think about some kind of scrutiny approval process before these liabilities are used and perhaps some funding based on risk. The next one is a civil service pension obligation which is in most of OECD countries a big problem. Basically pension when you have a contract is defered pay and if there are no funding but if it is just pay as you go it can be quite a lot of money. So this is happened in the nineties so OECD countries started to close down their old programs and create fully funded programs and move them into the private sector systems. These should just be recognized and be put on the books. However, some countries say that if you put it on the books you limit possibility for future change. Now for workers that have a contract and so on it might be very difficult to change this, but if you look at the social sector, social pensions for old day pensions and so on of course you can change it. And you might have to. If you look at the next slide you`ll see a little graph that shows you from the social pensions – how much is on the books and how much is implicit if things are continued the same. This is a percentage GDP and how much the government has in pension liabilities. I would not move to Spain if I thought that they have that many other taxes to pay for. The worst news on this account is that Italy recently went the other way. They had a funded program but they needed a cash so they took in liabilities, took in a cash and went over to a pay as you go system. So the opportunity and dilemmas are pretty great in this area. This is of course what you do with a Long-Term budgeting.

As the previous graph this one is also showing how sustainable are current policies and you might want to think about looking at that because it is very painful to change these things, these kind of rights and you might want a long implementation period and it might be very prudent to prepare politicians and a public for such a change. .

The next slide is about performance informations which is also a new thing or actually it is been around for quite some time but it is being implemented across OECD countries. And basically it is a movement to try to shift a focus from the budgeting people, away from inputs, away from appropriation, away from having a success criteria that says: well if we spend all the money than we've done our job and more looking at let's try to quantify, let's try to focus on what we actually get for the money we spend – number of students receive exams, number of operations and so on.

However it is difficult to define measures of performance. And they are not complete, they do not cover every thing and there are lots of changes too especially with political emphasis. And you need

some pretty strict audit mechanism to make sure that performance information is actually correct. And the basic problem is if a program shows that the performance of a program is bad, do you give it more money or do you cut the program completely. So there is not clear answer to that so it is information but it should not be used without some kind of the evaluation. But it is there to stay and audit institutions play very important role with this. To say when you are doing value for money audits, look at the performance that is how you determine this and to see whether the performance system is actually functioning and giving people the information that they need. I think that is what I wanted to say this time, I just want to add that one size does not fit all and these are general ideal type situations so they have to be adapted to the local destination and we also try to emphasis that transparency and good budgeting is not a destination you arrive at and then all is good. It is a movement and there are no Supreme Audit Institutions that are done that are ready. It is a continuous process. Thank you very much.

Mr. *Igor ŠOLTES*,
President of the Court of Audit, Slovenia

SYSTEMS AND INSTITUTIONS TO ENSURE THE INDEPENCE OF AUDITORS IN SLOVENIA

According to what we have heard today, I get the feeling, that once this Institution is established, the pubic would expect a lot from it. The Institution would cover the control of the public funds expenditures in all its segments, beginning with the state, local community, public enterprises, political parties, and all those who dispose, directly or indirectly, of public funds.

It should be pointed out at the start that this would definitely not happen at once. The Institution would not become a prodigy, in other words a miracle that would save Serbia from irregularities in the field of public funds. The establishment of such an Institution does not happen over night. It takes a certain time, which is impossible to speed up; it is impossible to be faster, at least in the so far experiences of the countries with a long tradition. Certain circumstances allow this.

Things said this morning were very important. The establishment of the Institution is not of much use without the determined sets of rules regarding the use of the public funds, envisaged either by the Budgetary Act, or Budgetary Law and Financial Law.

Without them the Audit Institution has nothing to audit, in fact, it can not audit the regularity of the business operations, for there would be no grounds for the audit. Provided, of course, that there are no laws. I would point out, at the start, to another thing, which seams a little disturbing.

There are no journalists present now. At the beginning the first speakers mentioned that the Audit Institution should have a lot of teeth. This means it has to bite and look intimidating. This is not the best way to put it; there is probably a better one.

So, those who dispose of the funds must be afraid. When a report is elaborated, heaven and earth should be moved, not in vain, but in order to get the report's conclusions realized at the end. Things are not that simple.

If you take a look at the European standards, the top Audit Institutions differ in their jurisdiction relatively. There are states in which Supreme Audit Institutions have the so-called sanction power. This implies that they can, in a way, punish the culprit financially. There are much more examples where the Supreme Audit Institutions do not have a repressive role, because it falls under the jurisdiction of different authorities. The Police, Public Prosecution Office, and of course, Misdemeanor Judge and Courts.

It should be emphasized that at the beginning of the work of this Institution, and even after 10 years of its performance, that the expectation from its findings and reactions would always be much bigger then the reality and the actual world. This Institution would never have enough employees, who could cover all the participants, or would be capable of reacting to, or respond to everything that could happen and that was happening so far.

I am not referring to Serbia only, but to the other countries as well. For instance, in Slovenia, where, I could say, we have a so called gap of expectation. Naturally, if we have close to four thousand subjects representing the actual subjects of our audit, it is clear that in the course of one year, which is the duration of the years' plan we are not in position to audit all four thousand of them.

It is impossible that things could change here.

What I would like to warn of, and what would probably happen is that the expectation regarding this Institution would be too zealous, too passionate. I deem, moreover, that these expectations should be moderated. Moderated and, at the start, one should build this Institution normally and without big fuss, or big bang, because this will not happen.

If the media and the public expect this, the Institution would very soon have a major break down, because, like I said, there would be more problems than this Institution would be capable of solving. Like I have mentioned, and as presented in the proposal of your Law, this Institution is not a repressive one. This means that it can not prosecute anyone, its principal power, however, lies with its reports and, of course, the media. The media conveys its message, opinion and findings to the public.

And the public is the one that on four-year basis punishes the irregularities in the elections. What was also mentioned, and was not pointless, was that the establishment of this Institution would take some time due to the problem with finding qualified personnel.

The problem of the experts or the auditors who would be trained enough to work and perform the audit in the most qualified fashion. Like the esteemed professor said earlier, by all means, the audit or the one performing the audit must have knowledge of a vast segment of rules.

This means that there should be enough experts covering all those segments.

The odds are that a certain time will be needed to have the employees trained so that they could normally cover all their duties or jurisdiction attributed to the Institution.

One should not forget that the audit is not only an appraisal of a balance sheet and income statement. It represents a beginning of a very important regular business operation. And at the end, the thing that the taxpayers expect the most is the performance, moreover, the output, effectiveness and the success of the business operation.

At the end they are interested if the state allocates their funds in a successful and efficient manner. That is the ultimate question that top audit institution need to answer to.

Everything else is, in a way, a hypothesis that enables them to give a final answer to this subject. This part of the audit, my colleague would probably agree with this, represents one of the most difficult parts of the audit, because this performance can not be successful, efficient or effective if, on the other hand, the public sector has no set forth goals.

In another words, if it has no set forth long-term and short-term goals regarding the purpose of the budget and funds given at disposal and management.

This morning the relationship with the Parliament was discussed a little, and the position of this Supreme Audit Institution. It is very important; we shall demonstrate this on the example of the Slovenian Court of Audit, that this Supreme Audit Institution stays independent.

This means that it does not depend on the daily politics or the elections. Otherwise each political party would make a team tailored according to their requirements, which would mean that the basic sense of objectivity would be lost.

The budget represents a mirror of the government. Like the budget, like the mirror of the government. Not just in financial terms, but in goals the government wishes to achieve with the budget. For example our ... Court does not look at the budget solely on the basis of income statements and regular business operations, but on the basis of the so

called output and efficiency and success of the business operations. In order to see this in a right way, we expect the Government and the Ministries to have an elaborated method of planning of expenditures with all the necessary indicators, the monitoring system, and a report explaining how they did it.

Without this, it is hard to give any opinion regarding a success or a failure. Trust me; people are especially interested in this part. That is, whether this system is successful or not.

I will refer to the problem of internal audits or internal control. It represents a system that requires a long period of establishment, if not even longer then the period required for the establishment of the Supreme Audit Institution. The Supreme Audit Institution represents an entity that is connected, intellective, but has one headman. Internal audits, or home audits are extremely divergent. They do not have one organization, one leader. They must have equal rules, but the problem is that even when the system of internal auditors is established, the question is frequently raised as to whether these internal auditors are adequately placed.

That is, whether they are... part of the managers' team or just executors of the tasks given by the managers' team. They must not become the fire brigade of the day. That is to solve and put out the problems made by the management. They have to resolve certain issues that have financial consequences. As one might expect, to use their know-how and experience to warn the management of the actions that would turn to be irregular or ineffective.

I would like to say few words about the groundwork that facilitates the independence of our Court of Audit, and that is the key issue. Our Court of Audit is defined by our Constitution. The Constitution and the Court of Audit Act bound the Court of Audit.

I will mention only what the Court of Audit Act defines. It defines the status of the Court of Audit, our autonomy, independence from other state authorities, our rules of procedure, the transparency of our work, and that each year we submit the report to the Parliament for its consideration. The appointment, dismissal, and the term of office of the members of the Court of Audit is also defined, as well as the organization, jurisdiction and performance, financial and material operations. Resources for the work of the Court of Audit represent a very important issue. We give the proposal of our own budget to the Parliament according to the procedure that goes trough the Ministry of Finance as a coordinator. The Ministry of Finance asks if we would

be kind enough to give the proposal of our budget. We present it, and if there is another one, which is usually the case, we try to harmonize the remarks. However, it is important for one's independence to have its own budget. That is, not to depend on the Government. This is very important, and especially in terms of expenses related to employment of personnel.

The largest portion of the budget these institutions spend goes on their employees. If one is not independent and autonomous here, than the institution can not be successful.

The name of our court is the Court of Audit. Maybe someone will find it a bit strange, but it is not so. The European Union has the European Court of Auditors. In France they have the Court of Accounts („Cour des Comptes"), and a respective Court of Accounts („Corte dei Conti") in Italy. Having a title is not enough. Regardless of the name given to the institution, the title should be backed up with the things that are tangible, its work, expertise and its reports. The problem we are facing is that we are regarded as a Court. And it is automatically expected that we will pronounce sentences. Due to the fact that we do not pronounce sentences we are sometimes experiencing problems with interpretations that we are more of a preventive authority with preventive competence and good for report elaboration, rather then the Court which passes rulings.

Our distinguished professor of criminal law, who is now a judge in a Court in Strasbourg, said that the Court of Audit is like a guinea pig. That is, it is neither Guinean, nor a pig. He was just being affectionate, so to say.

Few more remarks regarding the status of the Court. The National Assembly is appointing the members, and the Court answers to the Commission, and the National Assembly. I should mention that we send each our report to the Commission for Budget Supervision, Budget Control and Control of Public Funds. The Commission is entitled, if it decides, to discuss each report and give its remarks. The National Assembly is, therefore, very important to us. It is trough the Commission that we give our proposals for the amendments to the law. So far we have been relatively successful in this field, for we succeeded to change few important laws which proved to be arguable in practice. One of these laws is the Political Campaigns Financing Act.

This Law, i.e. the changes made as a result of our estimations that the financing of the political campaigns was not defined in a way which would allow the transparency and the collection of data that

would permit us to give an opinion that would represent a factual state in a at least 80%.

Speaking of the employees, you will see a chart showing how the trend of the employees began to expand since 1995 when we started to work. That is, in 1995 when our Institution was established, we had 40 auditors. Now, twelve years later we have less then 90 auditors and the overall number of our employees is 136. This process was gradual. It takes time to find each new auditor, regardless of the field of its expertise, legal, economic or IT.

If an auditor comes from the private sector, it takes him some time to adapt to the system, particularly because of the regulations as well as the approach pursuant to which the Court of Audit operates. Above all, when we talk about the performance.

As far as the financing of political campaign is concerned, it was always like this and it will always stay that way. There is no doubt about it. It remains uncertain whether the control of the financing of these campaigns is objective, independent or not. The other assumption is that the rules which define the method, limit and sanctions, that these rules are clearly set forth, and that they prevent, as much as possible, the political parties to look for pitfalls in the law. Also, to try to dodge the rules which require that they present their income in their respective financial statements.

What should be the subject of the regulations that govern the financing of a political party or election campaign? The issue, which is very important, is the definition of the election campaign, and what are its respective costs. If this definition is too narrow, trust me, each party will, regardless how big it is, find numerous reasons to present certain expense as a campaign cost, even though it has nothing to do with the things envisaged by the Election Campaign Act.

We have been living in this 21st century for seven years now, the century in which the technique is advancing very rapidly. Internet and other ways have somehow surpassed the definition of expenses in terms of advertising etc. That part, I am not referring to your example, should have been changed. If a definition is made in a way to count all the expenses to the letter, the law and the transparency can not win. The definition of election campaign costs must envisage that the expense is everything related to the election campaign, regardless of the method and means. The purpose is important. What counts is that the intention was to spend the funds for the election campaign regardless of the form.

Someone may say that this is hard to define, but it is worth trying. What should be defined is where the election campaign begins, and where it ends. Also, who can organize the election campaign, and who is responsible for it? The important thing is to make a register of the election campaign organizers no matter if it is at the state or at the local level. This is important in order to follow the number of the reports received by an institution. Possibly the State Audit Institution would be in charge of the collection and audit of the financial statements.

Moreover, the way the election campaign is financed, and who supervises and controls the performance of the election campaign? In Slovenia the Court of Audit is in charge of this. What I wish to explain is that this must be an independent and professional institution, no matter how it is called which has no political elements in its structure. Moreover, that it has no contacts, or connection with the organizers of the election campaign.

What needs to be done is to define penal provisions in case a violation of regulation occurs. I would like to emphasize that it is very important to limit the costs of the election campaign. This means to limit the amounts that could be given to the political campaign either by the physical or legal entities. Above all avoid the coalitions between the capital and politics. There is a relative danger that the economy or companies might ensure their future position trough financing of political campaigns, and some even said that the politics was nothing else then the dust thrown into the eyes of the citizens by the capital.

The financing requires clearly defined limits, which would enable the control and have sense. If the limits are not set forth, I do not know what the supervising authorities will control at all. The portion the party gets from the budget according to the number of the votes it won in the elections depends on this.

The report is important also. It is the groundwork paper that the Supreme Audit Institution disposes of, if this Institution is in charge of the control of the report and the regularity of the financing of political parties. Everything depends on this paper. This is what the Supreme Audit Institution gets, and it provides relevant information according to which the Institution prepares its opinion. The question might be raised as to what would happen if the Supreme Audit Institution is warned by the media saying: „The report states that the cost was 100 thousand euros, but we know that the billboards and the rented train, together with the airplane that flew carrying those advertisements cost more then 100 thousand euros“. Meaning, someone is cheating here.

Then the Supreme Audit Institution says – Sorry, but we only have this paper which binds us. It would not hurt to amend the Law giving the Supreme Audit Institution, or some other supervising and independent authority, the jurisdiction to conduct its own investigations, gather evidence and make a final report according to this material. The reports made by political parties are pitiful. It is vital to make everything transparent, who financed the political campaign and to what extent, no matter if they are physical or legal entities. This is the only way the control would be possible, because without this it would only be a peace of paper.

Let's look at the subject of the Supreme Audit Institution's Report in our example. We monitor if the organizer of the election campaign has shown the amount of funds raised and spent in the campaign correctly. If the funds were properly raised, in terms of limits and if they were spent in conformity with the regulations. Same as here, a special transaction account is opened where the money comes and from which everything is being paid. No bypass.

Only according to this, once the limits are obtained, together with the guidelines, and calculations, only then can we give the amount of the refund the politicians, i.e. political parties are entitled to receive from the budget.

I hope you got the information that would make you frown and incite to change the Law.

Kurt GRÜTER,
Director of the Swiss Federal Audit Office

CONDITIONS FOR A SUCCESSFUL AUDIT: AVOIDING OVERLAPPING TASKS BETWEEN CONTROL ORGANS, COOPERATION WITH THE NATIONAL PARLIAMENT

Preliminaries

When taking a look at the Community of States, you will soon realize that there is no such thing as the system of supervision. Roughly, three basic types can be distinguished: That of the supreme court of auditors holding judiciary power, called Napoleonic Model, or a supreme court of auditors with no judiciary power, and, third, an independent audit authority, the so-called Westminster Model. Each system of supervision reflects the respective political system. In a centralistic state, the supervision is bound to look different from that of a federally structured political system. In a system based on the concept of majority and opposition, the audit authority will set other priorities than in a multi-party system. And, last but not least, the people's voice also plays a major role in a direct democracy such as Switzerland.

Criteria for the independence of a supreme financial supervisory organ

No matter what type of supreme financial supervisory organ and its scope of application, what's important is the degree of independence. By the 1977 Lima Declaration, INTOSAI determined the standard of independence to be met by an audit authority in order to guarantee that it can act objectively and without reservation. Accordingly, an audit authority must possess organizational, functional and financial independence from the entities subject to its audit activities, in other words from the government and its subordinate administrative departments.

Organizational independence prevents the entity subject to auditing from exerting influence on both the internal structure as well as the professional careers of the auditors employed by a state audit authority. Above all, there must not be any opportunity to have the heads of an audit institution removed from their positions arbitrarily, say as the result of an unfavourable audit report.

Functional independence is intended to ensure the audit authority maximum autonomy in drawing up the audit program and, yet more important, to protect it from being prevented from carrying out certain audits by the executive authority.

Finally, financial independence aims at ensuring that the state audit authority is granted any financial resources required to perform accordingly, this meaning that it needs to be able to apply for funds directly to the parliament. Neither the minister of finance nor the government should be able to exert influence on the audit program by means of funds assignment.

Responsibility for protecting a financial audit authority's independence as its most important asset lies primarily with the parliament as the legislative authority. It is required to prevent any attempts to manipulate the audit authority's performance by the government, and to arrange for ensuring its independence by creating adequate legal protection against violation thereof.

The role of Parliament

You asked me to focus on interrelation and cooperation between a parliament and its audit authority. Let me start with a few basic remarks. The position attributed to the financial audit authority within a nation's legal and power structure can be considered an indication as to the degree of its democratization.

This correspondence between democracy and state auditing is not merely a result of pure coincidences, but is based on the duties and responsibilities inherent in a financial audit authority: controlling a state's income and expenditure leads to control over the officials responsible for managing public funds. And they are, ultimately, the members of government. Obviously, financial control is restricted to financial matters and does not involve political control over a government and its subsidiary executive authority. In a democracy, political control over the government lies with the parliament as the people's representation. Not only does the power to determine the budget lie

with the parliament, but also that of financial control, and thus the true leadership in a democracy. On an operational level however, parliament does not exercise this controlling function itself and would indeed not be in a position to do so – at least not in every area. Instead, it relies on the activities and reports of the financial audit institutions. Thus the downright symbiotic relationship between a parliament as the supreme bearer of sovereignty of financial control and the state audit institutions becomes plausible.

The more effectively a state audit institution operates, and the more rights and inspection powers it is granted, the more sustained and effective a parliament can put to use its sovereignty of financial control opposite the government and its members. On the other hand, the power of a control institution and the extent of its rights depend on the parliament's persuasiveness vis-à-vis the government. In nations with comparatively weak parliaments, the status of the control institution tends to be a subordinate one, whereas powerful parliaments will have a vital interest in potent state control institutions. This proves the aforementioned connection between parliamentary democracy and control institution, and also our earlier statement that the institutions of state financial control offer strong support to the parliamentary system and to democracy. For without their audit activities and reports, a parliament would not be able to exert its financial and hence its political control sovereignty over the government.

The position of the Swiss Federal Audit Office (SFAO)

With the awareness that only an independent audit office can exert effective supervision, the Swiss Parliament granted the Swiss Federal Audit Office (SFAO) the required independence. The institutional independence of the SFAO becomes apparent in that it establishes its annual audit program autonomously and is free to reject any special assignments issued by the government or the parliament if, by taking them on, the full implementation of the audit program might be endangered. Besides, it is entitled – and obligated – to publish its annual report containing the main focuses of its audit activities and any important statements and evaluations. It can also publish individual audit reports. It deals directly with the parliamentary commissions and the Government as well as with all administrative entities and organizations submitted to its supervision.

The independent status of the SFAO calls for a special organizational constitution to make sure it can in fact perform without being influenced. The framework intended to provide independence is ensured by:

- Appointment of the Director by the Government followed by approval by the Parliament.
- Director's competence to appoint entire SFAO staff and to take any other personnel measures.
- Drawing up the SFAO's annual budget by the Federal Parliament without the budget proposal of the SFAO being cut back by the government.
- The Director determines the inner organization of the SFAO autonomously.

Cooperation of the Swiss Federal Audit Office with the Federal Assembly

With its federalism and the two-chamber legislature system, Switzerland is virtually caracterized by control pluralism. Given the tight audit resources and the broad range of supervision, an efficient coordination is crucial. In this context the SFAO holds a key function.

The cooperation of the SFAO with Parliament is close and diverse. The primary contact is the Finance Delegation which consists of members of both chambers. It is authorized to issue assignments to the SFAO, takes note of the annual program and annual report of the SFAO, and discusses the individual audit reports. The SFAO sends the reports complete with all related documents and including the statement of the audited entity, to the Finance Delegation. The Federal Audit Act settles the relations and the cooperation with Parliament, such as the order that the SFAO can be called in for the preparatory organs' negotiations on budget and the Federal Accounts accounts and on individual credit requests. Furthermore, the SFAO is authorized to deal directly with the parliamentary committees.

In order to prevent an instrumentalization of the Federal Audit Office for political purposes, orders are given to the SFAO via the Finance Delegation. In other words, an expert committee must address its requests to the Finance Delegation and convince it of the importance thereof. The same applies for individual members of Parliament.

The Finance Delegation studies the requests and orders and hands them on to the SFAO if indicated.

In the two-chamber system of the Swiss Parliament with its numerous supervisory committees, a coordination of the various audit activities is essential. Therefore, the Federal Assembly has established the Conference of Presidents of the Control Committees (CPC), in which the boards of the various supervisory committees and the SFAO are represented. It meets semi-annually and coordinates the audits and inspections.

A special case: the supervision of the New Rail Link through the Alps (NRLA)

Currently, Switzerland is about to carry out a unique infrastructure project which is ambitious in every respect: rail tunnels through the Alps are intended to bring Northern and Southern Europe closer together. With a length of 57 kilometres, the world's longest tunnel has been planned and is now under construction. The total costs at current prices are estimated at 16 billion Euros. Numerous participants are involved in this project: railway companies, constructors, and the lead ministry. The railway and construction companies have their own internal and external audit bodies. In addition thereto, the ministry of transportation also carries out certain supervisory functions. The SFAO disposes of vast audit competences but also coordinates the various audit organs, since the avoidance of interruptions or double-tracks is crucial in this complex project with a construction period of over 20 years. Besides, the SFAO also supported the lead ministry in working out detailed controlling and reporting directives.

For over ten years now, the SFAO has been performing an accompanying financial supervision. Each year it conducts two or three audits on the two axes. In the initial phase, the emphasis of the audits lay with the service contracts, as those were not yet consequently competition-oriented in the first years and transparency was restricted in certain cases. The examined order placings regarding large contract sections of over 100 million Swiss Francs showed that the principles of competitive order placing and of transparency were observed and that the contracts were administered properly. Numerous recommendations were related to transparency and comprehensibility in transaction processing, their implementation leading to enhanced stability of the law so that the risks could be reduced accordingly.

Cooperation with the finance inspectorates

Parallel to the developments throughout the past 20 years in the private sector, implementation of a clear distinction and task sharing between internal and external financial supervision has taken place in public administration as well. On the initiative of the SFAO, the task of internal auditing in the case of a number of selected entities has been increasingly organized in the form of functionally autonomous and independent finance inspectorates. The SFAO is in charge of supervising the finance inspectorates. This task essentially consists in monitoring the effectiveness of their audits. For this purpose, the annual audit programs and all reports must be sent to the SFAO, and it is to be informed without delay of any shortcomings of fundamental or considerable financial consequence. The SFAO may also issue technical instructions. In addition, it has to ensure coordination between its own audit program and that of the finance inspectorates. Finally, the SFAO is responsible for training and advanced training of the staff of the finance inspectorates. As part of a cross-section audit, the SFAO is currently analyzing the mode of operation and the effectiveness of the finance inspectorates. Depending on the outcome, the SFAO will issue a recommendation on how to enhance internal revision in the federal administration.

Cooperation with other supervisory authorities

Efficient audit activity also means that double-tracks are to be avoided and the audit activities of the various supervisory authorities do not disturb the work processes of the party being audited any more than absolutely necessary. Therefore, coordination between the SFAO and the Parliamentary Control of the Administration (PCA) was institutionalized and the exchange of audit programs stipulated.

The findings which the SFAO makes in the course of carrying out its audit activity are intended to contribute towards optimizing the administrative processes. It is therefore required to inform the appropriate cross-section offices on findings going beyond the SFAO's field of responsibility, such as shortcomings in organization, task fulfilment or legal bases, so that they can take the necessary steps towards improvement. This primarily applies for the bearers of cross-section processes such as finances, personnel, real estate and IT.

Correlation with the Cantons

The cantons dispose of vast financial autonomy. Hence, they are free to choose a financial supervision according to their own ideas and requirements within their sphere of influence. With the numerous tasks financed jointly by the Confederation and the Cantons, cooperation with the cantonal audit authorities is particularly important. In view of the large amount of federal contributions to the Cantons or being handed on by the Cantons, an arrangement has been made in the Federal Audit Act which takes into account the federalist structure of the Swiss Confederation and the Cantonal administrations as well as the Confederation's legitimate claim for an appropriate way of supervising the use of these funds.

According to the Federal Audit Act, the SFAO has got the authorization of independent auditing in the Cantons, provided there is a legal basis for supervision by the Confederation, and the SFAO in particular, for the field of activity in question. If there is no such norm, audits may still be carried out, provided the cantonal government agrees. Cooperation with the cantonal audit authorities, and the SFAO's power to delegate certain audit tasks to them, are provided for in the Act.

Cooperation with the cantonal financial audit authorities has been increased and extended continuously for the past few years. At the annual conference, subjects of common interest such as financial perequation or audits in special areas such as community health are dealt with. Audit standards and methods in the fields of transportation, income tax or higher education are dealt with in common workgroups. And, finally, commonly financed projects are audited by mixed audit teams. This cooperation has proven very valuable and emphasizes the leading role of the SFAO in public financial control.

And who audits the auditors?

Allow me to conclude by addressing this frequently raised question, which is to be seen in close relationship with that of the independence of a supreme financial audit authority.

The question „Who audits the auditors?“ is indeed frequently raised. The vast independence and extensive autonomy of a supreme financial audit authority calls for a very special commitment, that is to say the commitment to a professional, transparent and efficient performance. And Parliament has a right to know how the audit author-

ity operates. It needs to be able to rely on the fact that the audit activity is based exclusively on objective and traceable criteria. Now the SFAO also wanted to conduct a self-critical assessment and therefore decided to undergo a voluntary examination. After checking various alternatives, the SFAO settled for a „peer review" or „audit on same eye-level", an approach also recommended by INTOSAI. The Bundesrechnungshof, the German federal court of auditors, agreed to analyse the SFAO's method of operation. Among others, the question as to whether the SFAO carries out its statutory assignment professionally and effectively and whether a surplus value for the auditee is generated, was dealt with. This examination turned out to be a win-win, since it permitted the SFAO to further optimize its processes, while the Bundesrechnungshof profited from the insight into another authority's modus operandi.

Conclusion

Each nation must decide for itself which financial audit model meets the needs and requirements of its parliament and society best. It is essential that the principles for an independent financial control authority determined by INTOSAI are adhered to. Worldwide experience shows that only an independent financial audit institution is in a position to effectively support a parliament in its supervision of the executive authority. While the parliament is to provide the framework and the legal premises, it can, on the other hand, also count on professional support in the form of the audit activities by the supreme financial audit authority. Whenever audits are not offered one-stop, attention must be paid to coordination among the various supervisory authorities. In this, the supreme financial audit authority holds a key role and is to take the initiative, regardless of any particular circumstances. Cooperation on same eye-level is no doubt more promising than the authoritarian approach.

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TIPOLOGY OF CORRUPTION IN PUBLIC PROCUREMENT

I would like first to thank the Anti-Corruption Counsel of Serbia, the Swiss Embassy, and Basel Institute on Governance for inviting me here to talk in front of you today about such an important issue as public procurement. As is already spec before, from three or more speakers, so I'll try to make it a bit shorter, although, as I said, public procurement is an important topic and we all know that bribery in public procurement has multiple negative effects leading to unnecessary economic and sometime dangerous projects so public procurement is definitely a risky area for corruption and bribery. So three major reasons that can be discussed are:

The first one is that public procurements obviously engage a lot of money, a lot of financial funds, and the average in OECD countries we considered that only for public procurement is approximately 15% of GPD. And I'll give just another example. In France, for instance, it presents 9% of GPD that is involved in public procurement. The second reason why it is a risky area is because public procurement is a complex process with many different actors. And the third reason is that public procurement is at the intersection between public and private sector and that is another one risk of corruption.

So, we'll see in a very simple way that we observers and actors for the fight against corruption found useful to draw a typology of risk factors in public procurements that allows in a second time to prevent, and control and combat corruption in public procurement.

So what are these risk's factors? The first one concerns regulations. In some countries we still see that there are no regulations or very week regulations, or inadequate regulations on public procurement. And on the other, on the opposite, you have complex legislations and changing legislations. That's, for instance, we faced recently in France after the adoption of the EU directive in public procurement that for almost four years we changed the code of public procurement three times. So we used to have a code of public procurement quite complex than

quite stiffed. And because of the transposition and adoption of the EU directive we had to change some parts of it and the commission was not happy with that, we had to change second time. And during these last two or three years, there was a kind of uncertainty in the public procurement code and so many actors were a bit scared about doing tenders because they didn't know which code or which legislation they have to follow. So we see if you don't have a regulation, you have a risk, and if there are too many regulations or changing regulations, you also have a risk.

The second risk factor concerns different sectors. We know that certain sectors, such as energy, infrastructure projects or weapon or arm industry are more vulnerable than others to corruption. And the third risk factor is one which is related to human resources. We know that also such lack of training, absence of culture of integrity, lack of rule of law in a country, or poor or week judiciary system, are also very important risk factors that can explain corruption in public procurement.

Where do you find corruption? It's quite easy to say that in each of chain of process flow you can face risk of corruption. It starts by the identification of needs and designs of tender. Obviously, procurement agency can formulate requirements which favors specific terms, specific company. It can also constrain market access to specific suppliers. So in the finish of tender this is the first step. You have the second step and it is during the bidding procedure itself. For instance, you have what we call non-competitive procurement, single source procurement, so in that case you have multiple reasons for that. You can say this is for national security interests. You could also say it is an emergency so you do not need to have a competitive procurement and obviously in that case you have a very strong risk of corruption. You have also framework contracts. Framework contracts very often are designed for goods and services. You do it also to save time and money and you eliminate numerous bidding processes by making a restrictive, competitive bidding and in that case you have a pre-qualification of vendors and obviously that was another risk of corruption. During the phase in which the winner of the contract is determined – what we call the contract award – you may also face corruption. Obviously there is a lack of transparency, for instance, when the bid is maybe publicly opened and at that stage you can have a manipulation. The absence of objective decision criteria or inadequate weighting of various criteria is another way to influence awarding process. You can face, for instance, in our country, that the costs of the tender is not the only criteria. It is often

found that technical features of the proposal, also the fact that it mixes community requirements or the time required for the implementation can be given excessive, poor, or no consideration according to the case and so the cost of the tender is not the only criteria. We are thinking, for instance, in France, of promoting SMEs, small and medium-sized enterprises, in a local or region. So if you want to promote certain type of company, SMEs, small and medium, that can be also criteria – objective criteria but not the economic one.

So there is there also a risk, for instance, behind the argument that you want to fight against unemployment in your region. So you are going to say I want to choose this SME instead of the big company coming from another region or another country. So there is also risk and very high risk of corruption for non-economic reasons, for social reasons. And obviously you have rules to prevent these models and also to avoid that the evaluation of the bid is left to individual. You create a commission or comity that is responsible to take the decision. Of course, within the comity you have to be very careful how you compose the comity and how effectively it carries out its duties. After the contract award procedure you have the contract executions, and during the contract executions you have also a lot of techniques to hide bribes so you can give a fictitious work, you can inflate the work of volume, you can change orders, you can use lower quality of materials, than that was specified in the contracts, you can supply goods adjusted to lower price or lower quality. There is plenty and different ways during that stage that also lead and go towards fraud or corruption.

During the execution phase new corruption challenges may also emerge with officials threatening to withhold payment unless they are remunerated by the percentage of the contract – so they don't pay as far as they do not get a bribe. In such case official delay due payments and due bribe payments can create serious liquidate problems for the companies. So the bribe is not at the beginning it is at the end.

Procurement and corruption in procurement can indeed be associated with other type of crimes. And they are distinct and must be differentiated. The main irregularity obviously in public procurement is bribery but we can also have other type of offenses, and legal offenses, called in certain case, offenses against equal access in respect of public tenders. You could have what we call in French translation – I do not know if it exists in Serbian criminal code – unlawful taking of interest. More classical crime can be associated to bribery in public procurement such as money laundering, frequently associated because in most basic form money necessary to bribe may consist solely of cash and in

these case you need to money laundry later. You have tax evasion, falsification of books. Any kind of crime related to count. Fraud is the most common. You have also what is called secret collusion between bidders during the tender. The most common collusive practice in public procurement in a bid is to coordinate the bids on procurement. Different companies may agree to suddenly common bids and than they decide which firm will submit the lowest bid and agree to rotate in such way that each firm wins an agreed number of valid contracts. Obviously the subcontracting, the way to recompense the loser is to subcontract to the losing bidder – that is the compensation mechanism. Another way, another crime related to public procurement is the irregularities in funding political parties and electoral campaigns very often associated with bribery and corruption. You use the money – the bribes paid during the public procurement by the company to fund your political party. This is the classic way that we faced in France during the 80`s and early 90`s. Many very mediatic cases of corruption was related to political funding and related very specifically to bribery in public procurement and in many cases corruption in public procurement involve conflict of interests. Common form of conflict of interest is self dealing. In such case private and public interest commute and official can hold interest in the contract. If it is not himself, it is somebody from his family. His spouse, his child, another close relative who can be, for instance, employed by the contractor or provide goods and services purchased by firm that is controlled by somebody from his family if not by himself directly. So how do we fight, first to prevent, and than to fight against bribery in public procurement? We all know that it is very difficult to tackle agreed or other individual or personal aspirations of bribes. So if we want to step towards the fight against corruption the public authorities can put in place a mechanisms to make corruption difficult, as the first point, to prevent the phenomenon and of course to settle determined measures such as effective sanctions or proportional and effective sanctions.

Concerning preventive measure, as I said before, we need clear and stable rules on public procurement. Public notice and forms must be available to any bidder. This is the place, for instance, in e-procurement[1] and using the neat technologies in order to help at least to get fair documents and transparent to any bidders promoting publicity and transparency. We need also competent staff, well trained, motivated if necessary and you may once well trained signed them ethical codes. You must inform them about the risk they face in case of breach

[1] E-procurement – electronic procurement

of duties. The procurement personal may be familiarized with the indicators of suspicions. You can have a list and a precise list of indicators of suspicious that may alert them to the occurrence of the corruption – when person responsible for bids unjustified high prices, if you have the reputation of the company, a late delivery and unusually high volume of purchases proved by a single procurement official. If you see close relationship between the official and the vendor and explaining increase of wealth or lifestyle of the official, all these different indicators may alert on the occurrence of corruption. Rotation of staff is also something important and the staff which is in key positions although you have to be very careful because in one hand you need well trained people and in the other hand, if you want them to make them rotate, you have to be very careful not to have new staff, you need to train again and again. So you have to find the right balance between well trained staff which means it needs time to work on the topic and also not to put the same person in the same location to long because we all know that there are bad habits that come after some time. You can use personal asset declarations even though that is also something you have to look very carefully because it's sometimes you could collect a lot of declaration but if you don't do anything with them; if you don't control them it's completely useless. And you could establish incentives to look for fraud or corruption within procurement authorities.

After these preventive measures that concern legal instruments and also the people who are supposed to implement these legal measures we have to focus obviously on control which is essential in order to prevent and to detect corruption. We all know that the investigations in public procurement are difficult and that they are even more difficult in the absence of control or in case of ineffective controls. Contracting authorities need to implement internal controls because when people are doing the internal control they have the necessary knowledge of administration regulations but they also have the knowledge of internal system of administrative work. This is something you can't invent you need to be part of the structure and to understand the way it works. The most control decision-making process as well as the procurement process, analyses of administrative organization may give indication who decides and how the project has been designed, organized and implemented. And the step of the definition of the project is probably very important as the following of the project. Very often when you control you focus on the procedure that was happening after the contract award but not much on what was decided before and in particular of design of the project where you can very much orientated the project

towards the single company and in the following of the project which is also a place where you can have a lot of corruption and very difficult to discover. For the verification of the procurement process can follow a check list, for instance, to ensure that everything is in good order.

Beside the internal control obviously you also need external control by external auditors that can provide also effective inspections that allow discovering significant deviations in government expenditure. If an auditor discovers deviation he should refer to internal investigators who may decide to transmit the information to judiciary. The judiciary may call for establishment of clear rules that require external auditors to declare suspicions that arise in review of the procurement process and in internal controls. Detection mechanisms must be promoted such as red flags or risks mapping. They allow providing tools to investigators. There is obviously the need to look closely, chronologically at all stages of the procurement procedures in order to identify problems which arise at each stage and in particular before and after the contract award. The collusion is frequent during the early stage, during the preparation and the design of the tender. However, since that corruptive path is secret and both sizes are in interest to hide it and that stage is very difficult to detect it. During the selection procedure some information may be contained by unsatisfied competitors but what happens quite often it can be obtained also by whistle blowers with anonymous referrals. And at that stage corruption is more easily detected and investigated during the contract execution. This is a bit easier because at that stage you may have somebody who has interest to blow the whistle or just to refer to what is happening. So in many cases the starting point of the investigation is almost always the complaint provided by private individuals or the losing competitor. In some cases, I'll give you, for example, France; the cases were discovered by tax officers that were controlling the accounts of the company. They saw the funny line and the line was written such as: Who you know. In France, that is Q S V – Qui Savez Vous, which means `who you know`. That is a percentage given to the political party. And that is how they detected it. We have also recently in France approved law that protects the competitor against prosecution if he provides to the judiciary information on breaches of duty in public procurement. It means that very often that it is a losing competitor who is been facing fraud in another company and if he go and say everything to the prosecutor it is not going to be prosecuted. This is something you can discuss but it is something quite apparently effective.

So the question raised is whether the corruption risks are increased by a stronger regulations or by more flexible procedures which can be justified by greater market efficiency which is right now the philosophy of the current EU directive that prefer to have the flexible regulations and in particular they leave the European countries free to determine the way they are using and they do the public procurement below a certain threshold. Above the certain threshold we are quite high for the EU directive – rules are more stronger but below these threshold they are quite flexible because they think it is up to the country to make its own regulation and they want it more flexibility because and we know by practice that if you have over regulated systems you generate more corruption because frequently the rules are overlooked. But at the same time if you don't have enough regulation than you are also susceptible to get high corruption so once again you have to find the right balance and I think and that is the philosophy of EU directive that the more flexible environment is preferable, is better but provided that you have severe deterrence and sanctions applied in case of violations. It means that you have to trust your judiciary system and you have to trust the justice of your country that is ready to take sanctions if you are not respecting the law. Otherwise, obviously a flexible regulation without deterrent sanctions without a strong judiciary it is not good. And it leads to more corruption. Just in very shortly now, to talk about the investigation in public procurement. They are very difficult. The police is usually not very well trained to investigate and you very often need well staffed team and multidisciplinary teams which not only police people but accountants, tax officers, you need the expertise of the people specialized in public procurement and technique expertise which ranges from engineers to architects, so wide range of skills to help the investigators. Obviously, you need to have in according to your judiciary system administrative and criminal sanctions and equally enforced and it goes up to a temporary suspension that can be implemented with great flexibility when appropriated but also with criminal investigations leading to prosecution and criminal sanctions that can be the strongest deterrent to bribery. Another important issue is the criminal liability of the legal person. Very necessary when it is very difficult to identify the person physically responsible of the bribery but you can always prosecute the company if you have these legal liability of the legal person, criminal liability of the legal person. I will just finish on the necessity, that will be mine conclusion, of homogenization of legislation and in particular on international level in cross-country tendering. We need obviously homogenization

of legislation and definition of the different pacts of the legal offences. That is why EU directive has dawn within European Union. We need a coordination of procedures, also with OECD convention against bribery of public officials and international commercial transaction. We have a coordination of procedure; we have a reinforcement of mutual legal assistance. We know that still mutual legal assistance remain slow sometimes difficult so we must work together to reduce these procedural and bureaucratic obstacles in order to have better fight against corruption in public procurement.

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TRANSPARENCY IN AND EXTERNAL CONTROL OVER PUBLIC PROCUREMENT PROCESSES IN SERBIA

For the first time after the Second World War, public procurements were regulated by passing the Law on Public Procurements, in July 2002. Thus, it is the initial date marking the beginning of existence of adequatly regulated public procurement system with the annual value in excess of EUR 1,5 billion. The system involves 12,000 customers and 80,000 tenderers annually concluding about 250,000 registered contracts. However, the number of concluded contracts is much higher, due to the fact that a number of customers do not submit to the Office their annual reports on concluded contracts. In that way, it can be estimated that over 1,000 contracts concerning public procurements are being concluded every day in Serbia.

The Law regulating such a wide and complex area of activities is a system legislation dealing with,practically, every part of public sector beginning with primary schools at the local level, all the way to major ministries, health and pension insurance funds, the largest public companies, etc.

So far, only the following two specialized institutions have been actively involved in the public procurement system: the Public Procurement Office and the Commission for the Protection of Tenderers' Rights, both established pursuant to the above Law.

However, this system has been designed in such a way as to include active participation of several institutions performing activities among themselves and, simultaneously, monitoring each other on the basis of „checks and balances" principle.

Since the topic relates to the issue of external audit and national audit office, I shall, in may presentation, skip the issue describing the role of Public Procurement Office, and focus on the national audit office, that is, on the external control aspect. I believe that my presentation on the importance and role of the national audit office

(NAO) in monitoring the legitimity of public procurement activities shall point out to the significance of existence of such an institution and the fact how much this kind of institution was necessary, as well as to the pressure felt by the only two institutions dealing with public procurements, the Office and the Commission – only for the reason of non existence of NAO.

The national audit office shall monitor all three phases of public procurement procedure. First, there is the phase of public procurements planning, which is considered to be an „open wound" in the public procurement system. Broadly speaking, planning is the key issue, not only for public procurement activities, but for the whole system of public finance. Further, NAO shall monitor the regularity of the second phase of procurement – procedure of selection of the most favourable offer. Finally, the national audit office shall check the third phase of public procurement – implementation of the contract.

In addition, the national audit office shall monitor the deferred payment procurements, such as credit and leasing arrangements, etc., as well as the so-called „confidential procurements".

As regards „confidential procurements", we have, during the previous years, witnessed the controversal domestic public debates concerning whether such procurements should be under control of the Public Procurement Office. However, the regulations related to the external audit clearly state that the Army and MIA are obliged to submit to the national audit office the data referred to procurements, which are considered to be governmental, military, or official secret, while, under the Law on Public Procurements, the Office is not competent to deal with this issue.

In the process of monitoring the regularity of the public procurement procedure, the first step is internal control. Offices of Internal Control should exist with each customer and should be the key mainstay for the national audit office in performing all its activities.

While checking the customer's procurement plan, the NAO shall firstly estimate the needs of the relevant customer together with subsequent checking of the estimated needs the relevant customer stated in its plans of activities.

Furher, the NAO shall check if the annual plan of the customer is in compliance with the customer's medium, and long – term plan, if the manner in which the criteria are defined is correct, and whether those criteria reflect the real needs stated in the plan. We are all aware of the significance of precise defining the criteria for efficient and effective meeting the needs of the customer and obtaining most favour-

able „value for money", as well as for providing fair competition and prevention of discrimination.

In addition, the national audit office shall check the transparency of identifying the customer's needs, transparency and precision of specification, such as, stating the producer's brand, as well as the estimated value of the relevant procurement.

When it comes to selecting the most favourable offer, the national audit office shall check if the selected public procurement procedure is appropriate, whether the implementation of tender procedure without prior announcement is legitimate, whether the effective competition has been provided, and whether the appropriate selection of criteria was made.

As concerns the performance of the contract, the national audit office shall monitor the implementation of the contract by checking each item to the contract during the life of the implementation of the contract. The customer's experience concerning the reliability of the delivered goods, works and services, as well as complaints, quality, servicing, etc., shall also be monitored. Therefore, monitoring performed by the NAO shall cover almost whole process of procurement, starting from the initial plan up to the completion of implementation, with the possibility to precisely determine whether the contracted product has actually been delivered, both concerning the quantity and the type and quality of product, as well as the effecting payments and eventual non-compliance with the provisions of the contract.

From all the above stated, the negative effects of non-existence of the national audit office have obviously been present, particularly if we refer to the regularity of implementation of regulations in the field of public procurements in the course of previous four years – abuses in the public procurements sector are no longer present in the medium phase of the procedure, which is under the control of the Office and the Commission, dealing with selection of the most favourable offer, but, instead, they are evidently present in the first and third phase, that is, in planning of customer's needs and realization of contracted procurements.

Documents under direct control of the national audit office shall be: procurement plan, complete tender documentation, minutes from opening of offers, report on awarding the contract, decision on selection of the most favourable offer, and the actual offer of the selected tenderer. In case of request for protection of rights submitted to the Commission, the NAO shall check complete documentation related to

the protection of rights, such as, the contract between the customer and the tenderer, invoice, and the dispatch note.

Each non – compliance which could possibly appear in public invitation, tender documentation, concluded contract, or documents related to the implementation of the contract could initiate additional checking measures. It is obvious that only such, overall monitoring can produce a proper effect.

Concerning the public invitation procedures, the national audit office shall be authorized to monitor the regularity of defining the relevant criteria. This issue is of essential importance, since the practical experience shows that most of attempts to „fix" tenders are made due to discrimination in selection of the said criteria. Precisely, the NAO shall check the legitimity of the selected criteria, as well as the manner in which they are determined and weighted in tender documentation. Further, it shall check whether the criteria have been applied in compliance with the provisions stated in tender documentation.

The regularity and compliance of the contract components, such as prices and deadlines, with those contained in tender documentation and public invitation shall also be checked. In other words, the NAO shall check whether the public invitation, tender documentation and the contract comply with the provisions relating to price, deadlines, and other parameters, as well as whether the payment conditions are in accordance with the contract provisions.

The NAO shall also check if the customer observes the decision of the Commission for Protection of Tenderers' Rights on complete or partial cancellation of the contract, thus ensuring the observance of implementation of the Commission's decisions, which presently represents a significant problem.

In case of procedures without public announcement, the national audit office shall check the documentation stating the customer's explanation of reasons for avoiding public announcement, as well as the contract concluded pursuant to the selected procedure.

As concerns small value procurements which are usually not efficiently monitored, the NAO shall check the following documents: the decision on small value procurement, submitted offers, manner in which offers have been evaluated, the way of selecting the most favourable offer, and finally, the concluded contract on small value procurement.

The national audit office shall differ from other monitoring bodies in the field of public procurements in respect of instruments it shall

have at its disposal, if some irregularities in the customer's public procurement procedure appear.

Namely, the national audit office, after completing the monitoring process of the customer, shall make the auditing report pointing out to the customer to eventual irregularities found in the monitoring process. Customer shall be obliged to eliminate the irregularities within 30 to 90 days, depending on the nature of such irregularities.

In case the customer does not eliminate the irregularities in a satisfactory manner and within the prescribed term, it shall be considered that the principle of good business practice has been violated. The Law defines two categories of violating the principles of good business practice: smaller and havier violations. Depending on the category of violation, the measures to be taken against the competent person of the customer shall be determined.

In case of smaller violation of good busines practice, the national audit office shall submit the request for taking actions, to the body within whose competence the customer is, against the competent person of the customer, that is, against the director.

In case of heavy violation of good business practice, the national audit office shall notify the National Assembly, the Government, and submit the request for relieving the competent person of duty and notifiy the public, accordingly.

The experience of the countries with highly developed national audit offices shows that the above measures are very efficient.

The law on national audit office shall further provide that the body competent for relieving the customer's competent person of duty is obliged to inform the national audit office on its decision within 15 days from actual relieving the customer's director of duty. In addition to this measure, the NAO shall also be authorized to bring criminal charges.

From all the above said, it can be concluded that the national audit office is of crucial importance for the public procurement system in Serbia. However, there is a great potential for development of an efficient cooperation between the NAO and the two already existing institutions involved in this kind activities – the Public Procurement Office and the Commission for Protection of Tenderers' Rights – for the purpose of making monitoring process of public procurements more efficient. Cooperation among these three institutions could be realized on the grounds of exchanging information on noticed abuses, coordinating actions in preventing and revealing abuses, and rendering professional assistance.

In order the national audit office could be able to implement the efficient monitoring over the customer, the employees with specialized knowledge in the field of public procurements are needed. Having in mind the specificity and complexity of the issue of public procurements, the Office and the Commission could render an important assistance to the NAO in professional training of its auditors in respect of public procurements.

I shall conclude my presentation by quoting four, in my opinion, significant recommendations, stated by SIGMA in its Report on Public Procurements in Serbia for 2006:

- First, it is necessary to consider the organization of the internal control and external audit in order to ensure the integrity of the procurement process;
- Second, the Government should, in close cooperation with all important participants, prepare the strategy and plan of action for the reform of public procurements, clearly stating the measures to be taken;
- Third, the Public Procurement Office should be strenghtened, and
- Fourth, it is necessary to improve the customers' capacities, primarily by way of professionalization of people engaged in public procurement activities.

Saša VARINAC,
President of the Commission for the Protection of Tenderers' Rights

TYPOLOGIES OF CORRUPTION IN PUBLIC PROCUREMENT IN SERBIA

When we speak of category of irregularities in the field of public procurement in the Republic of Serbia, we cannot fail to notice the manner in which the Commission for the Protection of Tenderers` Rights, that is, the Commission for the Protection of Rights as it is called now, has been regulated and set up.

Director of the Public Procurement Office, who did not mention nor felt the need to mention the Public Procurement Office. Indeed, I believe that particular problems faced by the Commission should be pointed out, above all, status and organizational ones, which we have been trying to overcome for the last three and a half years.

Before I begin with my presentation, I would like to say a few words about the Commission and its activities. The Commission is a second instance body in the procedure of protection of rights, issuing a final decision on legitimacy of a particular proceeding of the public procurement which has been contested.

In the first instance, a decision on the request for protection of rights is made by the customer. It is a kind of appeal to conducted procedure, whereas in the second instance, the Commission issues a decision, which is final and enforceable.

The main problem is the way in which the Commission has been established. It is established within the Public Procurement Office. As a result, we have a Commission which is a part of the executive power monitoring most significant activities of that very executive power relating to expenditure of budget funds.

Above all, one of problems is a mistrust of tenderers expressed towards the work of the Commission. For the last three and a half years, we have tried to strengthen their confidence by acting objectively and finalizing accurately and promptly our work.

A question that I have often been asked at various gatherings was – whether there are any pressures on the work of the Commission.

I think that sufficient pressure on the work of the Commission is the legislative frame which provides for a very limited period of 15 days.

On the other hand, the Commission has neither its own budget nor its employees. Employees engaged within the Public Procurement Office are associates, advisors, who are assisting the Commission in its work and are of greatest importance for the Office.

With such organizational concept, it is difficult to act in a limited period. If I further mention that, at present, the Commission has five full time employees – advisors who are employed by the Public Procurement Office, then I hope you can get a clear picture of our position.

Namely, we are talking about enormous values, great political and financial interests, whereas documentation sometimes involves several hundred pages. In such situation it is very difficult to act in a given limited period of time.

At present stage, the Commission faces a particular problem in its work. Initially, irregularities were reflected in certain procedural errors of the customers. However, such errors are often made on purpose nowadays, they are sophisticated and reflected in the initial stage of the opening of public procurement, in the contents of tender documentation.

In that part, we keep encountering with the requests of tenderers disclosing the fact that certain technical characteristics are being „fixed", if I may say so, in such a way as to suit privileged tenderers.

Indeed, in such situation, the Commission does not have enough experience when confronted with such requests. But another problem is that, even if we apply and enforce the provisions contained in the General Administrative Procedure Act, which is a subsidiary in this case, and even if we engage experts, as we have tried in several cases, we can hardly expect to sustain accuracy and promptness in our work.

I don't know how much are you familiar with the manner in which our judiciary functions, for example, with the role for experts within it, and not only in judiciary, but also in functioning of some other authorities, administrative bodies. When you give a case to an expert in order to get a professional report and opinion, often several months pass before you receive a feedback.

We simple cannot function in that way as the Law on Public Procurement contains a provision stipulating that the submitted request suspends all other activities of the costumer.

That points to the need for urgent acting of all those involved in the procedure for protection of rights, therefore it is necessary to make

a specific list of experts, and to prescribe the obligation of ensuring prompt expertise, as well as to the need to regulate the issue of conflict of interests which was also apparent several times when we tried to obtain expert reports and opinions.

Namely, we had information that an expert, for example a university professor, was engaged to prepare tender documentation, which of course, is not banned. However, such person cannot be engaged in examining the case that is documentation which has been contested.

Also, the manner in which the Commission has been set up is an enormous problem. Draft of the new Law on Public Procurement provides for the setting up of the Commission as a separate government body whose members are to be elected by the Parliament. What we from the Commission feel as necessary is the experience of the colleagues from the region, the experience concerning comparative law and the court protection against the decisions of the Commission.

Namely, as already mentioned, the Law on Public Procurement does not provide for the submission of appeals nor initiation of administrative dispute against the decisions of the Commission. We believe that the administrative dispute should be introduced as well as a possibility for submission of complaint against the decision of the Commission, under one condition – that the procedure for public procurement proceeds upon the issuing of a decision by the Commission.

Thus, the decision should be re-examined at the request of interested party, and the ruling of Administrative Court would be an indicator of the way the Commission operates.

At the same time, the pressure on the work of the Commission would decrease, since it is not easy to issue decisions in proceeding against which there is no possibility of lodging any legal remedy.

We are aware that the errors of the Commission cause a lot of suspicion in such circumstances.

The Commission issues a decision either on approval of request for protection of rights, and partial cancellation, or cancellation on the whole, of procedure of public procurement, or on rejection of request for protection of rights.

In respect of reasons for cancellation of procedure of public procurement on the whole, the reasons are those existing in the initial stage, more exactly in the public invitation and tender documentation.

What is the problem with the tender documentation? By the way, tender documentation is a kind of a strange term – tender, although tender is not the substance of the public procurement – tender is a type of a procedure of the public procurement. However, since we have accepted such term, then we shall use it. Tender documentation contains all necessary data for making a complete, accurate, and sound tender. It is the basic act on the grounds of which the full procedure of public procurement is conducted.

Tender documentation can be divided into four basic parts and irregularities contained in these relative parts are the reason for cancellation of procedure of public procurement on the whole, and a costumer is instructed to repeat the procedure.

The first part contains Guidelines on how to make the tender and information on the method of submission of the tender. In case that part provides for a short period, or the period for submission of tender is not precisely determined, which also happens, then of course what we have there is a discrimination of tenderers, since the certain number of them, who somehow manage to get the information regarding the expiry period, are privileged. In addition, something else often encountered by the Commission in its practice, is an excessive amount which has to be paid for tender documentation. In several cases, tender documentation, consisting of around 10 pages, had to be paid for DIN. 50.000. – or even more.

It is one of the problems and an irregularity which discourages and dissuades tenderers to take part in the tender procedure. Another serious problem is indefinite definition of time limit and venue of opening of the tender. It often happens that the date and hour of opening of the tender are not precisely defined, thus, there is a doubt to what the precise date on which the tender documentation is to be opened is, the reason being that the customers, although they are under the obligation to determine the date and hour, do not do so, but instead, use a kind of descriptive definitions, number of days, thus creating a dilemma – what happens if the opening date falls on Saturday or Sunday, etc.

The Commission has the opinion that particular date and the exact hour of the opening of tender have to be precisely defined.

Also, an important part, if not the most important one, of the tender documentation are requirements for participation in the procedure of public procurement and the evidence evidencing (for) fulfillment of such requirements. Some of the requirements are often quite unnecessary, illogical from the point of view of public procurement,

thus, as a consequence, limiting, restricting, competition which is the most important and the key element in public procurements, as the Government aspires, more exactly it should aspire to create the most favorable conditions including wide competition, and by this means achieving the 'quality for money' principle.

Let me say that certain requirements which have often been encountered by the Commission, to be exact by the customers, are references which neither in quality terms, nor in quantity are in line with the customers' needs.

We recently had an example that for 400m of water-supply network, a reference from previous year for 40 km was required, which is absolutely unnecessary. Naturally, that procedure was canceled.

In the same manner, unnecessary approvals or certificates issued by particular institutions are requested, although such institutions are not the only ones, more exactly other institutions are entitled to issue relevant certificates which are also acceptable.

Further to this point, we frequently meet with undue and disproportionate requests in terms of business-financial and personnel-technical capacity involving the number of employees, equipment, mechanization which is actually unnecessary for the realization of public procurement.

The next part of the tender documentation contains technical specifications. As I have just said, technical specifications are the field where we are faced with the most serious problems. In the recent period, the largest numbers of requests have indicated that particular tenderers have been favored on the grounds of technical specifications.

How has it been done? Often, technical characteristics from a certain producer's catalogue are simply copied. What we have next, are the requests by the costumers that the different parts of certain equipment, which are not functionally connected, should be manufactured by the same producer, indicating some kind of favor towards a particular tenderer, and going all the way to the requests containing most explicit irregularities, in terms of stating the precise brand, type of product, or its origin.

The fourth parts of the tender documentation, as I would divide it, are criteria for election of the best tender. Criteria are used for ranking of tenders.

Once it is established that particular tender, more exactly, the tenderer which has submitted it, has met the requirements necessary to participate, and then the ranking of tenders is effected, or simply said, the appraisal by points is performed. The problem concerning that part

of tender documentation is undefined, non-existing criteria, undefined methodology for their application, the methodology being additionally devised and created offhand, at the stage of making the professional evaluation of the tender.

Equally, as with the requirements, we have discriminatory and absolutely illogical criteria here. One of the irregularities is also a modification of criteria at the stage of the professional evaluation of tenders, and the customer, although he has defined particular criteria in the tender documentation, does not comply with it later, but introduces total uncertainty into procedure and takes into consideration criteria not stated at the very beginning of the procedure.

What happens, although not so often, concerning the irregularities in the stage of opening the tenders is their non public opening, in cases when the obligation for public opening exists? Further more, there are irregularities, more exactly shortcomings, in making of the Minutes, which is of great importance, since the content of Minutes on opening of the tender indicates whether the tenders, at the moment of submission really contain everything that has been required.

Any dilemma arising later on, may be settled only on the strength of the Minutes on opening of tenders. If the same is irregularly made, if it has any defects, then the dilemma, whether there was any irregularity at the moment of submission of tender, cannot be settled.

Thus, it may also be the reason for cancellation of the procedure on the whole, as the procedure cannot be canceled partially, and the customer instructed to go back to the procedure of re-opening of tenders which have already been opened.

We have also had several cases with irregularities existing in all stages of the procedure. We have had a case where tender documentation was missing, there was no opening of tenders and where, later on, there was no report of customer on the professional evaluation of tenders.

In such situations, there is no dilemma for the Commission which, of course, cancels the procedure of the public procurement on the whole, if the request for protection of rights has been submitted.

What has to be said in relation to such request is that the Commission issues decisions exclusively within the limits of submitted request, so that the Commission does not have any competences concerning conducting of inspection and cannot spread the investigation to the entire procedure but only to such violations explicitly indicated in the request for the rights protection.

I have to admit that, so far, most decisions were issued involving partial cancellation, canceling mostly the stage of professional evaluation of the tender. When?

For example, in case of irregular appraisal of legitimacy, that is, sufficiency of tenders – whether any evidence exists, whether particular requirement has been met, the part of procedure of public procurement is canceled, or, to be more precise, the Commission cancels it, if it establishes that the application of criteria has not been effected in a manner prescribed by the tender documentation.

What also happens is that tenderers, although they request it, are not able to examine documentation on conducted procedure of public procurement, that has also been one of the reasons why the costumer is instructed by the Commission to go a step back in the procedure in order to enable the tenderers examination of documents and to assure them of the manner in which it has acted.

As I mentioned earlier on, the problems in the work of the Commission exist, however, there is also an enthusiasm felt by all of us working with the Commission to achieve adequate level of timeliness and objectivity in our activities.

The Commission for the Protection of Rights, established pursuant to the changes in the Law from 2004, has, so far, issued in total 1.240 decisions under submitted requests. What I would like to point out is, that the half of requests which were submitted and dealt by the Commission were approved, whereas the procedures of public procurement which have been contested, were canceled. Out of the entire number of canceled procedures, 1/3 was canceled on the whole, while 2/3 were partially canceled.

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THE RATIONALE OF TRANSPARENT PUBLIC FINANCES – IMPACTS ON ECONOMIC GROWTH

Empirical stylized facts

The research on the prevalence of corruption, on its causes and consequences, is in full swing. Thanks to the data that has been collected and provided by *Transparency International*, the topic is part of many research efforts worldwide, and a handful of results are available today. Let me present to you the most relevant empirical regularities in this domain.

Finding 1: More corruption is related to smaller per capital income (Mauro 1995).

In other words, corruption is more usual in poor countries than in rich countries. [More bullet points will follow on this list. Let me just quickly make a digression and show you this result in more detail.]

This chart shows the statistical relationship between the percentage of people who report having paid bribes in the last year, and the income per capita in the respective country. Note that the vertical axis is logarithmic, so what we see here is not a linear, but more or less a hyperbolic relationship. This means that very poor countries typically have very high levels of corruption, but countries somewhere in the middle in terms of per capita income already have rather low levels of corruption.

The following slide makes the connection between wealth and corruption maybe even more obvious. [Slide with graph by *Transparency International*] What we see here is the distribution of the corruption perception index (CPI) as published by *Transparency International*. The map looks almost like a map of poverty. The correlation is not perfect, there are exceptions (Chile, Italy...), but the connection is still very clear.

William Easterly, the famous former Worldbank economist, has put it concisely when he said:

„The rich have markets,
the poor have bureaucrats."

Actually, maybe it is not the bureaucrats perse; maybe it's the fact that they tend to collect bribes that makes them harmful, so one might also say:

„The rich pay prices,
the poor pay bribes."

Let me show you some more results that have been found in this empirical literature on corruption. Each of the following results has been published in one or several scientific articles, and if you are interested in the sources, the references are available.

Finding 2: More corruption is related to less equal distribution of income (Gupta et al, 2002).

It has been found that an increase in corruption acts like a degressive tax, thereby redistributing wealth from the bottom to the top.

Finding 3: More corruption is related to weaker public finances, in the form of higher debt and lower per capita tax revenues (Tanzi and Davoodi, 2000; Tanzi, 2002).

It has to be expected that tax revenue is weaker since corruption is correlated with low income. But this effect is still there even after controlling for income. The reason is simply corruption of tax inspectors. If they can be bribed, tax revenues that go to the legal state decline, although the tax burden of the citizens may only decline a little, since the bribe really is just part of the tax deal.

Finding 4: Corruption reduces private investments of all forms. It reduces financial and physical investments (Mauro, 1995; Brunetti et al, 1998, Wei, 2000), as well as the formation of human capital, in the form of education or health care (Mauro, 1998; Gupta et al, 2002; Tanzi, 2002).

This is probably the most severe effect from an economic development point of view. Corrupt governments seem to spend less on education and health care. Private individuals seem to reduce their investments as well, just like foreigners. Corruption is not a good business climate because deals that rely on it are much more difficult to enforce, should one side decide to renege on a deal. This heightened uncertainty is no good news for business.

Finding 5: More corruption is related not only to lower average income and higher poverty, but also to lower trend growth rate (Mauro, 1995 and others).

There is a distinction between the level of income per capita on the one side, and its growth rate on the other. The negative relation of corruption with the growth rate has been found by several authors, but is less pronounced. Moreover, there is an important exception to this finding.

The big exception: East Asia

In a recent article, Michael Rock and Heidi Bonnett (2004) find that the negative correlation between corruption and investment and between corruption and growth is conditional on region and size of the respective economies. In particular, the effect of corruption in the larger East Asian economies – China, Indonesia, Korea, Thailand, and Japan – seems to be reversed. The smaller, industrialized or newly industrialized East Asian Economies – Singapore, Hong Kong, and Malaysia – have developed with very small amounts of corruption, but this is not true for the large countries just mentioned.

It is of course not possible from such a small sample of countries to pinpoint the exact reason for these different experiences, but the authors are able to tell a convincing story that seems to make sense. They argue that the question whether corruption is detrimental to growth depends on the domestic organization of corruption. If corruption is performed individually, by many independent bureaucrats, the result is effectively to impose an extremely high tax rate on citizens, which is bad for development and growth. The authors cite many African countries as well as India and the Philippines as examples. If, on the other hand, there is a strong central state that exerts control over the whole corruption network, the outcome then depends on the time horizon of the top executive.

If the top executive has a short horizon and the power to monopolize the corruption network, the effect is disastrous. The authors identify some Latin American and some African economies with this situation. They call it hyper-presidentialism, in which a strong president faces only limited constraints and checks, and where business-politicians turned presidents simply loot the nation as long as they can.

If, on the other hand, the government has a longer perspective, it will behave like a patrimonial monopolist and organize good deals for the economy as a whole in exchange for kickbacks. The authors argue that this is a way in which corruption might actually be beneficial for development, and they cite the large East Asian countries as examples of this strategy.

Which way does the causation go? – Endogenous institutions

So, with the exception of some major East Asian countries, corruption is associated with smaller income per capita, slower growth, and weak investment. It seems reasonable to assume that there is a causal link that goes from corruption to weak development. Some econometrics tests have indeed verified that this is the case (e.g. Gupta etal, 2002).

New theoretical research, however, points towards the possibility of reverse causation as well (Bruegger, 2005). Corruption may not also be one of the causes of low growth, it may also be due to low growth.

The idea is the following: if people expect low growth in the future, the property rights they have today is not worth very much. Why invest in factories or education if prospects are bad? In fact, factories and a good education are not worth very much in such a circumstance.

So if property rights are not very valuable, people will also not try very hard to defend and protect them. They are much more likely to accept weak or even extortionist institutions. If, however, property rights are valuable because growth prospects are good, then the people who hold these properties will fight for good institutions, for „institutions of private property“ as Acemoglu et al (2001) have called it.

Conclusion

Weak institutions facilitate corruption, and corruption is bad for growth, which makes property rights less valuable. For this reason, people will accept weaker institutions, which then again facilitates corruption. This makes corruption is a self-enforcing process and a vicious circle. The bright side of this is that combating corruption can

induce a virtuous circle, that makes it more and more easy to improve the functioning of the public and private system.

What do you need to fight corruption? You need the political will to do it. The political will to do it will emerge as soon as a sufficient share of the electorate is interested in good institutions. As long as this is not the case, successful political parties will only pay lip service to this aim, because there is no political capital in this topic.

A significant share of the population will be interested in good institutions only if there is a sufficiently broad middle class. I was told yesterday and the day before that this is currently not the case in this country.

What is the middle class? My personal definition is this: it is people who have some property to lose (and who are therefore interested in property rights), but who still have to work for a living.

Serbia's economy will grow – I think there is little doubt about that; Serbia is on a catching up path. The question is how this additional wealth will be distributed. If everything goes to a few tycoon families, Serbia will become a new aristocratic society, with a large working class and a small aristocracy who owns everything – very middle age. I think, or I hope, that this will not happen.

I think it is more likely that the wealth will ultimately spread, and a middle class will actually emerge. When this happens, the high days of corruption will be gone.

Now, if it is indeed true that Serbia has no middle class to speak of today, then realistically, I am afraid, we are talking not about years, but about decades for this process to complete.

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KEEPING THE BOOKS CLEAN IN THE PRIVATE SECTOR – PREVENTING CORRUPTION IN PUBLIC LICENSING

Yesterday we discussed the laws used in the area of prevention, control and in the institutions a lot. Today I would like to share with you the experience I gained in the years while I was working in different fields, both in the sector of accountancy and audit. I believe there is a lot to we can share and I am of the opinion that we have a lot in common.

When I began to work, I wanted to work in the area of forensic investigation of companies, but I must admit I did not work much in this field. There were neither will nor readiness in Slovenia to tackle these issues.

When I was with the „Deloitee &Touche", as an Auditing Company we performed forensic investigations, but they would usually end before you knew it, and results would not be disclosed, so there was not much good from it.

Let's take a closer look now at what corruption actually represents and what we are talking about. I have prepared two possible definitions. Published works, moreover, are full of them. You can find a lot that could be interpreted as corruption. I prefer these two, because they do not speak of money. In fact there is no mention of money in these definitions. They are more about the actions, which are unfair and encourage preferential treatment.

If we consider the corruption as broadly as this, then it would probably be a lot easier to fight against it. In Slovenia, whenever the corruption issue was discussed, and whenever the scandals occurred and we tried to finish something, we always had problems establishing what actually happened. More than that, how to prepare the procedure and present evidence that someone took money.

As far as I know little has changed here. The more refined and not so hard corruption is still present, there are always a lot of interconnections and acquaintances where favors are being made, which in

the end, however, amount to money. Let's discuss what it is that we are really fighting against. I believe that it is very important to know that everyone engaged in cooperative business, governmental bodies and public companies wish for different economic fields and funds as well. It is, therefore, important for all of us to bring more transparency into the work of the private and public companies, to elaborate the financial statements in a fashion understandable for everyone. Also, to have well defined laws. We should make the work of the institutions dealing with this area equally transparent and competent as well.

The issue that is probably more important then good laws is to raise public awareness of these circumstances. We have many laws in some fields in Slovenia. We thought that the laws were good. Then we changed and improved them for the better. At the end, we got into a circle with numerous detailed laws. Eventually, however, it all comes to our wish to do everything by the book, it all comes to form, and no one thinks of the essence.

Believe me you will never be able to write a law free from pitfalls and possibility to get around it. You all know that we are extremely good in finding faults in laws and make things look a little bit different.

I recall when I began working with an international organization that some American Consultants came. They said to me: „We will teach you how to deal with the inflation." I said: „No way, we are pros compared to you, when the inflation is concerned, and in finding ways to dodge things."

I would like to emphasize once more how important it is to begin talking of the essence instead of the form. Because, usually, every procedure fails when the form is the focus of a discussion, everyone looks for pitfalls in the law, and not what actually happens in that area.

There is also one important area I feel we should change and develop, and that is the public awareness of ethics and moral in the business world. There are still many shortcomings in this area in Slovenia, and I believe we will have to work on this for a long time.

If you observe the institutions shown in a slide, which could contribute in this area, I think they show the situation from Romania and Bulgaria. You will notice both governmental and NGO institutions capable of fighting against corruption and contributing to transparency and the elaboration of better financial and other statements.

I was shocked when we started working closely with the international institutions and when we tried to put in order some issues in Slovenia. You are probably not aware, because even in Slovenia some people employed in the economy sector had no idea that Slovenia was

still not a member of the OECD. Also, that Slovenia no longer has the majority of international organizations, like USAID, because we are now more developed and we do not need them.

In Slovenia, however, the World Bank and the IBRD never did much. The IBRD is present, but it all comes to granting some loans, and they are not that active. In the past two years I was a part of a group that tried to establish the Transparency International and we still did not achieve this. Therefore, there is not much actual will that those international organization, which work in this field enter Slovenia and make some changes. Also, I did not bring you various analysis made in Slovenia recently. Moreover, when we made analysis in the past years, it was amazing how the managers from private and public companies responded to all the changes that we needed to adopt, both because the of European Union and the instructions we had to follow.

One of the important instructions is to improve the performance of the Supervision Committees and various monitoring institutions, and to begin elaborating Code of Ethics and Conduct both in the companies and governmental institutions. Over 52% of the managers of the leading Slovenian companies are of the opinion that this is pointless and that they need no codes in their companies.

I believe that this points out that we are not yet aware that our conduct should be changed, and that different conduct rules should be observed. It was also interesting when we adopted this Code in Slovenia, which is now mandatory for all Joint Stock Companies on the Stock Exchange. The Stock Exchange accepted the Code; so the companies have to sign statements that they will uphold these rules and act accordingly. I think we adopted this three years ago, and it was unbelievable how much were the major companies against this. First statements were incredible. „We do not want this, we will not observe this. The Code requires more than the Law and this is none of our business."

Everyone knows that the Code requires more than the Law. That is why we have the Code. Otherwise, we would not need it for we would put everything into the Law. I believe that you are probably going to change things in this area. There is lot to be done here.

It is important, when discussing public and private companies as well, to achieve certain transparency and to elaborate the financial statements and annual reports in a way that an independent individual could count on them and trust them.

The way the company communicates with the internal and external public, i.e. the suppliers and others is important for fulfilling

this goal. Inside information, as you all know, are important for good management of the company, but also for good work of the Supervision Committees in the companies. External information is important for owners and public.

I believe that the situation here is not much different, and that you have basic laws and that they probably resemble those in Slovenia. I would like to warn about one thing. I do not know if you have changed this, but we are experiencing lot of problems. Also, the European Union instructed us to change this quickly. There are still some public companies and institutions that receive their funds from the budget, they are spending the budgetary funds, and applying the old Law on Accounting. We have not yet changed this. They work on the basis of a „cash flow".

That is, they do not follow the accounting standards; instead they work on the basis of the „cash flow". This may lead to problems and non-transparency in the work of this public companies and institutions, but also with the budgetary institutions. Just now we had local elections in the Counties; however, the same old story took place. When a new County Chief Executive enters his term of office and takes over the County, everyone is shocked to see that the County is in fact working poorly. That its income is not as expected, and that the new County Chief Executive is in no position to do anything in the next two years, because he would be busy paying back the debts and obligations previously made. Until this is settled, they really do not show transparent financial statements with normal income and expenditures. We are having major problems in this area.

Another thing, we do not like to talk about it a lot, and I believe that you have similar problems. We have not yet managed to elaborate a complete balance sheet for the state and local authorities. There are still a lot of buildings and funds necessary for the infrastructure, which the state has not yet included in its balance; things are not yet cleared up, and we do not know what belongs to the state and what to the local authorities.

There is much to be done here. Until we do this, I believe it would be difficult to speak of transparency, public funds, when the crucial element is missing, i.e. balance sheet specifying factual property registered in books.

The companies, moreover, use the accounting standards. There are Slovenian, and international accounting standards. Differences are not huge, but there are some. We have a „double bookkeeping" and it

is not very transparent. There are times when a reader can get confused while reading these financial statements.

Our Company or Enterprise Act has changed again, and now it emphasizes transparency a lot, and the way financial statements, annual reports are being made.

I will not talk about the Law on Public Procurement, because we discussed it yesterday, but I will mention that we have changed it. The new Law on Public Procurement entered into force now, because the old one gave us more and more difficulties.

As I have said before, we considered the form instead of the essence. The former Law prescribed such things that disabled the normal working process. For instance, when the Minister wanted to fly with an airplane, a tender would have to be invited, and the best bidder would have to be chosen to sell the Minister a plane ticket. It was really foolish.

Now we have harmonized the Law with the European instructions and we know when to invite a tender, and which rules to observe. The problem, however, will still occur if we disregard the essence, or consider the form only.

We are loosing a lot of time in all the public tenders due to this Law. I do not know how much does your TV covers news from Slovenia, but lately we had many problems. We are building a hospital for three years now, and buying its respective equipment. No public tender, however, can be invited because someone always complains and things are getting nowhere.

On the other hand, we had many examples where it was obvious that something was wrong with our public tenders. It was clear who was chosen for some major state projects. After the complaints were launched, the documentation was changed. First it was blue, and now, all of a sudden, it turned green. So, the best bidder was degraded and was no longer the best bidder, and it was plain visible that this was the case of corruption.

The problem is that nothing happened. When this repeats more then once, then no one takes it seriously any more. Also, we recently had problem with an Army Procurement. We had an international tender, and at the end the conditions of the tender were changed.

That it was very important to follow the rules and prevent corruption, it would be good if you could achieve this. In our case it turned out that the agreement was made to buy a number of special tanks, but

the price was specified for 60 tanks only, and 25 tanks would cost, as much as they would cost.

The next issue that would probably surprise lot of Slovenian companies, both private and public, is the new Law, which entered into force just now.

I am referring to the Law on Private and Public Joint Ventures. We made many changes in the area of the public procurement and in the area of concessions as well. I think the people still have not realized what this Law contains.

In Slovenia we have concessions in different areas, but Law did not govern most of them. Different areas were covered by different rules.

Moreover, we have concessions in the field of education, and private schools as well. Concessions are given for one year, a definite period of time according to the extent of the fulfillment of different levels of educational programs, and no one is paying for this.

We also have concessions in the field of the exploitation of natural water springs. However, payments are made only for the exploitation of the springs for bottled water, and not when they are used for wellness centers and spas, or similar. This has to be changed.

Also, we have concessions in the Health Care Industry. The case is similar; nothing was paid here as well. The concessions were given outside public tenders, so it was impossible to give concession to legal entities, only to individuals or other special institutions.

Now we need to change the new Law completely and invite public tenders in this field, and to repeat the whole muddle and give concessions again. I believe that order will be established in this field once this Law is applied.

If, at the end, we look at what we are to do exactly, I think it is important to agree how the public would react to this, how to fight the corruption together, and how to find good and week companies, public enterprises, and managing directors and entrepreneurs as well.

We are still witnesses of a widely spread nepotism in Slovenia. Yesterday someone mentioned whether it was good for a Managing Director to have a son employed with the company under his management. Or, that an officer from a public sector or a Minister has its relatives positioned close to his. There are lots of examples like this, and the question is when we are going to introduce Codes of Conduct and Ethics in all these fields again. Then the fight against this would be a lot easier.

I find it interesting; I am not talking of Slovenia, but of Germany and data are not exactly fresh. Slovenia, however, is going trough a last

minute transition, we usually say „in the very nick of time". Moreover, a problem of interlocking emerges very often.

What does interlocking represent? For example, it represents a union of several companies in the region, whose CEO's make a pact. One of them becomes a Chairman of the Board of Directors in his company; the other is appointed a Chairman of the Board of Directors in his respective company, the third in his, and so on, until the circle is closed. In Slovenia we have a popular saying „Gorenjsko na vezo", where we have one bank and several companies interconnected in such a way that it is impossible to enter their circle.

They hold the property; they own all the Supervision Committees and everything else. It is clear that business operation in this circle can not be transparent, that everything is possible here, and that lot of money goes trough these companies, creating situations prone to corruption.

A would like to give you an example; maybe it is not the right one, of the Company „Bonijar". They represent a major Publishing Company in Sweden, which holds practically a majority of Swedish media. This could result in serious violations of their respective Code of Competition, but they have been doing business for about 200 years, and have a firm Code of Conduct regarding the business policy and practice with clients, and political parties.

Their Regulations explicitly envisage that, if a person from a Company becomes engaged in politics, he has to withdraw from the Company, i.e. to have no part in the share of the Company. Also, the Company has to restrain from doing business with his respective political party.

This is, I believe, a fine example of how business can be managed, without the presence of the monopoly or some rich clan. I will not refer to them as tycoons, but they are extremely rich. It would be nice if the media could do their work transparently in all the cases like this as well, without corruption and scandals, etc.

Finally, what are the odds that something could be done? I believe, if we start respecting the essence instead of the form, if we discuss our laws openly, and if the judiciary works transparently, if the public believes that we are really fighting against the corruption, then, I think, together with codes and mutual cooperation with other states we have good chances to move things into the right direction and achieve something in this field.

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KEEPING THE BOOKS CLEAN IN THE PRIVATE SECTOR

Few people are able to realize the significance of precise and reliable financial reporting, particularly when fighting against corruption is concerned.

Reliable financial report of legal entities performing activities within the private sector is not only a precondition for protecting interests of investors, creditors, government, employees, and the public, but also represents one of the instruments for preventing corruption.

The question is – how can precise and correct maintaining of books and financial reports prepared on the basis of such books, contribute to prevention of corruption?

In my opinion, there are two ways for influencing the level of corruption by way of financial reporting. If the books are correctly maintained in the private sector or elsewhere, those who are inclined to be corrupted shall be discouraged, since the transparency of performing activities, which will result from correct maintenance of books, shall represent one of the obstacles for corruption to appear.

On the other hand, correct maintaining of books shall enable less difficult detection of transactions correlated with corruption. In the Republic of Serbia, financial reports of companies, nowadays, present information which are, in my opinion, much less reliable than they were five years ago.

According to the data given by the Centre for Credit Standing with the NBS, even 52% of total reports, submitted in the, so called,written form to the above Centre, contain formal errors – errors in mathematics and calculations. Therefore, it can be said that, in balance sheets, assets are not equal with liabilities.

This percentage would, probably, be higher, if there was not for the electronic form of submitting reports where the possibility of making such errors has been eliminated.

Even 5 to 6% of total number of legal entities do not submit their financial reports at all, although they are legally bound to do it. As far as

I am concerned, these data reflect the attitude of the Government and private sector, primarily managers, to the issue of financial reporting.

It can not be understood that a manager can be able to sign an incorrectly prepared report, not even formally. On this occasion, I shall not speak about the crucial errors, that is, about wrongful estimation of positions which do not comply even with the basic legal requirements. In my opinion, this is a serious signal for the Government to take this issue into consideration.

If we pose the question – what caused the decline in reliability of financial reports? I think that there is a number of causes, and would like to point out to three of them.

First, I think that, in 2002, we accepted international standards too quickly and used them as major basis for financial reporting. To avoid misunderstanding, I have to say that there is nothing wrong in accepting International Accounting Standards. On the contrary.

I have always pointed out that the acceptance of international accounting standards can improve the quality of financial reporting in Serbia. However, such transition to these standards implies certain prior preparations which, in this case, were apsolutely avoided. The point is not in their inadequacy, but in their non-existence.

Second cause is in our under-developed auditing profession.

Third cause can be found in not realizing the importance of financial reports.

When I said that the decision of applying the standards was made too quickly, I meant that, at the time of its making, we did not even have the Serbian translation of International Accounting Standards.

However, the Law on Accounting and Auditing implies that „the financial reports should be prepared in accordance with the IAS". When the accountant asks: „Excuse me, but where are these standards?", you can give him only the English version.

It took us a year to make a translation. That is a serious, diffucult, and responsible task. With much efforts, we managed to provide a good translation.

When I said that the decision was made too quickly, I had in mind one more thing. You make a translation and burden the accountants with the obligation to learn these translated standards. When? The Standards have thousands of pages. How is it possible for an accountant to master the issues required by the standard in such a short time?

We can say that we had the advantage since our 1996. Law on Accounting and Auditing was to the great extent adjusted to the

provisions of the fourth directive of the EU. Thus, the knowledge our accountants had was in accordance with the requirements prescribed by the International Accounting Standards. However, our accountants did not have knowledge on many other issues required by those standards.

They were not wrongfully educated, but they were and they still are, unsufficiently educated.

The additional ex post training was inadequate and of low quality. The material subsequently given to the accountants to instruct them in apllying the standards was not within the satisfatory criteria.

On the other hand, the Law prescribes auditing of all large and medium scale companies. I think that you will agree with me that the capacities of the auditing profession in Serbia are far from being sufficient for performing the auditng process in a proper manner. The number of companies whose reports should be audited and the number of authorized auditors is in large disbalance.

Finally, the latest Law prescribes the mandatory auditing to be made until September, at the latest. Sorry, but if I were an investor or a creditor, and if I receive the audited report for the previous year of the company to which I am supposed to grant a loan or buy its shares, in September, such report would mean nothing to me. I should be expected to sit and wait the first nine months for them to prepare the report on audit, in order I could rely on data presented in the relevant report. It is simply not acceptable.

There is no permanent supervision of the quality of auditing. We do not have organized monitoring system in our country which should be used in supervising the work of the auditors, and the criteria which they implement in giving their opinion. Naturally, I do not have firm evidence for this claim. But, when you often hear from several sources that the opinions are often given, even without seeing the companies, only on the basis of the reports, that is, without visiting the relevant company, then you have serious resons for having doubts concerning every opinion given by our auditors.

What was the Government supposed to do, but failed ? It is quite clear to me that our country, like many other transitional countries, is facing the numerous problems and that financial reporting is certainly not our priority. But, due to its significance and influence on other sectors, my opinion is that financial reporting should be much better treated by the Government than it has been up to now.

When I say so, I have in mind the fact that it took us three years to amend the Law on Accounting and Auditing, for which it was obvious, immediately when it was passed, that it had serious defects. Those defects were pointed out to, but three years had passed before only some of them were eliminated, by way of passing the new Law.

If we evaluate the position of the Government concerning financial reporting by considering the quality of employees with the Ministry of Finance who are supposed to have certain knowledge in accounting and financial reporting, I have to say that the evaluation is unfavourable. Ministry of Finance have one person dealing with the issues of financial reporting and two or three young associates. For such a task, it is necessary to have a serious team of people who will deal with these issues. Such task can not be, and it never has been, entrusted to only one person, but, today, situation exactly reflects such conditions.

All this led to the customers' loss of confidence in financial reports and, naturally, caused the social status of the accounting profession to rapidly decline. Today, when you say that you are an accountant, you are considered as someone who does not now anythning and is not needed at all. Believe me, you can, even today, find directors of companies who consider maintaining of books, preparing reports, as an unpleasant obligation incurred to them by the Law.

They do not consider maintenance of books and presenting of information as an opportunity to represent their company in the best possible manner. No, it is something that must be done, and they shall do only that what is required from them, not a bit more. I am afraid that we shall not move forward as long as the attitude and position concerning financial reporting do not change.

The Law on Accounting, passed in 2006, as an amendment to the Law from 2002, represents a small movement ahaed. The new Law defines the standard basis of reporting. The Law from 2002, presribed that the standards had to be applied everywhere, meaning that even a person at the counter was obliged to prepare financial reports according to IAS, which was realy an absurd.

The 2006 Law divides companies, that is, on those companies with the obligation to maintain the books, and the enterpreneurs and small firms who are obliged to act in compliance with the Rule Book, which is not the best solution, but better than before when IAS were applied. Medium and large scale companies are obliged to apply IAS.

The Chambre of Auditors was founded with the task to monitor or take care of the quality of audits made, that is, to make efforts in

improving the auditing profession, as a whole. This is, of course, to the benefit of all.

The basis for founding the National Accounting Commission was made, with the assignment to monitor the observance of EU directives, which we do not have, as well as the International Accounting Standards and International Auditing Standards.

What are the items that the Law failed to prescribe, that is, those items which remained as a problem. The problem of translation of those standards remained. Take a look at the site of the Ministry. You will find the following wording – the standards prevailing until 2003. Now we are in the year 2007. From 2003 until 2007, a large number of standards was applied, a lot of new standards were made. I wonder what are the grounds on which our accountants, our companies, prepare their reports. Do they prepare them on the grounds of standards prevailing until 2003. This is something that can not be tollerated. Only because the Law, neither the new, nor the previous one, does not define the party responsible for making translation, for verifying translation, and finally, for determining the term within which the translataion shoud be presented on the site. All this must be specified by the Law. This issue can not be left to be negotiated and agreed upon. It must be clearly and precisely defined.

Further, the professional positions are not adequatly regulated by the Law. The Law on Accounting defines only the professional positions in the field of auditing. To avoid misunderstandings, I must say that I have nothing against auditing. On the contrary. But the fact is that the quality of financial reports and maintaining of books does not depend only on auditing. I suppose that people who are engaged in these activities, that is accountants, have to be educated and authorized to be able to perform their activites.

Now, according to the Law, the books can be maintained by anyone. No certificate is required. Nothing. The Law does not specify the professional position of the accountant. There is the authorized auditor and authorized internal auditor. Accounting profession, at that level, is absolutely left to professional organizations. To conclude, the legislator failed to regulate that part of accounting profession.

In my opinion, the regulation of particularly that level of accounting profession is of great significance for precise and correct maintenance of books. Maintenace of books can not be entrusted to someone who does not fulfill precisely defined criteria. Besides, neither the Law nor any other rule of profession do not insist on the code of ethics. Accounting profession bears a great public responsibility and it

is of significance for accountants to observe the rules of their profession stated in the code of ethics.

But, since the Law did not define the criteria to be fulfilled by the accountant, the person maintaining the books is not obliged to respect the rules of profession defined in the code for professional accountants. Such a person can not be called to account for non – observance of the rules of profession, since the Law does not prescribe such an obligation.

I think that, in this respect, the changes of the Law are necessary. As I have already said, I think that we all together, including the Chambre of Auditors, the national audit commission, even medias, must be active in affirmation of the importance of the accounting profession and financial reporting. All the way until the majority accepts and understands that the decisions should be made on the basis of data which, not exclusively, but to the large extent, are provided by the accounting service, and that the quality of such decisions depends on the quality of information, we shall not be able to respect those who perform this task, nor to insist on performing these task in an appropriate manner. It will be all the same to us – let them do whatever they want. This is the problem which makes room for the corruption. When you have books which are not precisely maintained nor updated, wrongful financial reports, reports not checked by anyone, you can expect the appearance of corruption. Everybody can do whatever they want to, with nobody to regulate nor control anything.

What does the National Commission try to do concerning these mentioned issues? The task of the National Commission is, among other things, to make a strategy and the Plan of Action in the field of financial reporting. We shall have to see where we stand, compared to Europe, concerning the basis of standards and defining what has to be done to diminish, as much as possible, the existing gap. We shall try to propose to the Government to establish a separate professional body to be in charge of professional translating the standards, and updating standards, to avoid the situation in which we found ourselves today.

We should also try, through the Chamber of Auditors, to insist on improving the level of accounting profession by way of serious and permanent education and definition of serious criteria for acquiring auditing position.

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STATE'S AUDIT AND PRIVATIZATION

Ladies and gentlemen, I am very pleased to be here during these session which is devoted to so called transparency days. The International Organization of Supreme Audit Institutions – briefly INTOSAI – helps the audit work of the member institutions in many ways. Among them the great importance is attached to the learning from the so called best practices which are internationally adopted. This is why I first touch upon the guidelines on the best practise for the audit of the privatizations and then a little bit on the Hungarian privatisation and certainly on the guidelines on best practices for audit of risk in Public Private Partnerships. And finally again a little bit I touch upon a PPPs (Public Private Partnerships) in Hungary.

The craddle of the INTOSAI privatisation guidelines is the INTOSAI Working Group On Audit of the Privatisation. It was set up in 1993 and now forty countries participates in its work. Its terms of reference are to identify and examine problems confronted State Audit Institutions in the audit of privatisation, to exchange information on the arrange of the experience gained within the working group's membership in resolving these problems having a special regard to relevant work in INTOSAI regions. And the certain element of the terms of reference is to facilitate provision of information on the subject to all INTOSAI members. As a result of its activity the working group elaborated the guidelines in 1998. There are as perhaps you know available on the internet. They had launched aiming at putting guidelines into a very practise around the year 2000.

Privatisation can be defined narrowly and broadly. For the purposes of the INTOSAI privatisation guidelines it is defined narrowly as a transfer of ownership from the public sector to the private sector. A broad definition will be used that is the transfer of the service provision to the private sector in connection with the guidelines on the PPPs which will be soon my topic area. As regards the structure of the guidelines on privatisation eight area of particular concerns might be

identified. There are two guidelines for skills required by the State Audit Institutions. Second area guidelines which are general in character with some ten guidelines. Guidelines conserning trade sales, management, employee buy outs, mass privatisations, auctions, flotations, with some twenty five guidelines. And guidelines relating to the audit of the cost – there are four guidelines for this area.

In the case of the guidelines there are four parts to each guidelines. The first is the issue. The second is why the issue matters. And third the guidelines is given itself. And finally the reasons for the guidelines are given depicted in the text.

Instead of listing all the forty guidelines of some fifty pages which is quite impossible I present a brief guide to a privatisation of course based on guidelines.

Let's see know the guide to privatisation terms and concepts. As to the stages of privatisation we consider three stages in privatisation process. The first is reviewing options and preliminary timing. Here the primary task is to prioritise the objectives of the government in order of importance. Such general objectives might be for example raising money from the sale of the enterprise or moving towards market economy. Another might be selling very quickly. The mention objectives are rather short term by nature. Examples for long-term objectives are for example securing investments for the enterprise for long period of time or to remove it from a direct political control. Another task in the first stage is to evaluate the possible options by undertaking so called feasible study. If the study concludes that the privatization is the best way to meet objectives then the best method or methods must be selected for. In doing so according to the international experience the government may benefit a lot from the reports of the previous privatization made by the State Audit Institutions. The second phase is to undertake so called pre-sale considerations. Here tasks are to establish a good sales team, to appoint external advisers who are independent really of boss, vendor and potential bidders to avoid the conflicts of interests. And third task here is to undertake reforms and reconstructions if necessary. As you know it is often important task to restructure the enterprise which is to be privatized. It might be for example resulting in breaking down the enterprise into several units to be sold and managed separately.

Another important task here is to establish clear timetable. Then the pre-sale evaluation is an also important step in the privatization process. Here it is advisable according to the international experience to set floor price beneath which the enterprise will not be sold. And

finally of course defining the bit criteria is very important activity at the end of the pre-sale consideration process. The third phase of the privatization is the sale itself through the application of various methods of sale. The first type according to INTOSAI classification is the trade sale. It is generally used for selling small and medium size enterprises. Compared to flotation trade sales can normally be completed more quickly and have often been used in cases where the government want to introduce a new skills or new methods into the enterprise. The second type of the sale is the so called management employment buy-out. It is competitive version when one of the bidders is a team of the enterprise current management or employees. It is non-competitive version when a vendor offers a sale without any competition. The third type of the sale in our classification is the auction. It is a rare method of privatization. However, to sell many shops small businesses services are often used by the former planned economics in the Central and Eastern Europe. The forth type of sale is the flotation or public offering. They are generally used for selling very large public enterprises and some of the public utilities. They are most expensive and time consuming to carry out but then according to the trade sale which is not as much expensive but if this type of the privatization is done well they normally provide a greater returns for the vendor in the long run. Here I underline that the process of rotation needs badly the transparency. And finally the fifth type of the sale is so called vouchers sales which is known as mass privatization due to the effect that in the voucher sale very large number of the enterprises are privatized quickly at the same time and to a great many new owners who typically comprise significant proportion of the adult population sometimes up to eighty percent as it was the case in the Poland and in the Check Republic.

Having reviewed dominant features of the privatization process let`s have now a quick look to a generate auditing framework which provides a guidance about the best way to audit certain aspects of privatization. The basic question to be answered by the audit is this. Was the privatization a good deal meeting the requirements of the value for many principles? At level two the audit has to answer the following four questions according to the suggested methodology. Was the correct privatization strategy chosen? Second, was the privatization process well managed? Was the best price achieved? And is the deal likely to meet its objectives. But according to suggested INTOSAI methodology at the level three the issue for example the privatization strategy – which is the first issue or question at the level two – should be investigated further in details by the State Audit Institutions with the help of answers to the following questions. Were there clear objectives for

the privatization? Second, more detail question attached to the strategy issue is – were all possible options identified. Then, the third were the options properly evaluated. Then, was there clear basis for the decision adopted and so on. So I am not going to continue to put questions of third level relating to all four questions which you see on the slide but I'll just mention that in the methodology we elaborated for this there is again fourth level even put in more detailed questions concerning the privatization. So this is a detailed system.

That is what I wanted to tell you very briefly about the INTOSAI standards and guidelines and methodology. Now I would like to turn briefly to my second topic area – that is the privatization in Hungary. In two or four Hungarian State Audit Office completed a major summary evaluation of the effectiveness of our privatization program fulfilled for the period 1999-2003. The method of the evaluation used in this summary evaluation was consistent with the relevant guidelines developed by the INTOSAI working group. Now this is why I am going to mention some of our findings from this summary study.

Policy objectives of the privatization – which is very important issue – were based upon so called property policy principles adopted by the Hungarian Parliament and on the privatization law which was adopted in 1995. There were six general objectives I identified for Hungarian privatization process. They are the establishment of the market economy, the introduction of new modern technologies and methods of management – that was the second objective. The third was widening the circles of the players in the domestic markets. The fourth was development of the capital markets particularly with the inclusion of the foreign capital. The fifth objective was decreasing of the economic fall of the state. And finally we tried to maintain the employment level establishing jobs if possible. These objectives have in generally accepted by all Hungarian governments during the last decades, both liberal and the conservative governments. This political background was very supported for the Hungarian privatization process. It was also important political consensus behind Hungarian privatization that the privatization should be as fast as possible. In connection with this is the conclusion – now we may say that quick sells resulted in most cases with rapid gains in economic efficiency but low profits. In the cases of slow sales the profits appeared to be much higher. These experiences perhaps suggest that there were not enough spending state revenues on the reconstruction of the enterprises. Better to step it over.

Methods of the Hungarian privatization

Here the key question was – market focused versus voucher privatization. As regards to this question in accordance with the so called value for money principle we followed a privatization of market type. As to the second question foreign versus Hungarian investors we were from the very beginning in favor of the foreign investors in the Hungarian privatization process. There was special privatization packages offered for sale to foreign investors only. Their role was important in period 1991-1995 in particular when there was very strong revenue orientation and a strong reliance on the needed foreign capital and the investors. The third question to prefer financial or professional investors was to be answered. As regards to this question I have to say that there was no real policy choice between the two groups of investors. In the period 1991-1995 the so called strategic investors were rather investing in transforming and reorganizing the connection's structures of the companies and in enquiring potential market so they went to buy up the markets. This type of investors focused mainly on the food industry, retail trade and small and medium size enterprises. And later, in the second part of the last decade, they focused on energy and the telecommunication sectors..

Which methods were most used in Hungarian privatization process?

Tendering – the first method – was applied more frequently – some 53% share from the total number of the transactions. The second largest applied method was the method of sales to employees with some 24% share. But of course if we take the distribution according to the contractual value of the transactions, then the tenders represents only almost 39% and the capital market methods introduction to the stock exchange represent very high share 41% of the total and value of the transactions due to the very valuable transactions – energy, telephone companies and banks although the number of the transitions was just 5%. This was our new findings concerning the methods or techniques applied.

I want to draw your attention that in Hungarian privatization there was high ratio of foreign currency revenue – some 57%. Of course, it arrived actually in cash amounting to some 7.7 billion U.S.

dollars. It is huge money amounted to the some 31% of the total for the direct investment in Hungary. So the foreign direct investment came into the country through the privatization largely. The other part so called Greenfield investments represented some 69% – so the rest from the 100%.

In our summary report on the privatization process we made an attempt to estimate the balance of the privatization in Hungary. 2.600 billion Hungarian foreign property value projected to the level at the 1990 cost some 12.000 billion Hungarian florins as the result of the revalorization. The register transactions stood for some 56% and some 44% was the so called missing assets or property. So 56% of the total business assets of the state we could consider as registered transactions but we could not register some 44% from the total assets. From this 44% of share an estimated 35% could be explained with well articulated factors like loss of market value or property decrease due to very bad management. But some 10-15% of the property can not be reconsidered otherwise than actually missing property or value. This fact was a little bit shocking for us and particularly for Hungarian republic and started to seek for persons and institutions responsible for the missing property. But this discussion is sure now getting over and we considered that this missed assets is not high at all from international aspect. In other countries – of course it is very hard to make comparison for this – the miss property is result of the privatization process as it was experienced in Central and Eastern Europe is minimum the same or even in some cases according to our rough estimation is higher.

As a result of this very active privatization process there is a major factors of change of the register capital of the companies. In 1992 there was some 43% of the capital owned by private entities and at the end of the ambitious privatization process it end up to some 78%.

Now let`s have few words about the role of the State Audit Office during this privatization process. In audit activities of the state assets management agency and the public companies we presented opinion on their internal controls which was very important. They also presented opinion on their assets registry system. This registry system caused several problems during the privatization because this system was in a very bad shape always.

We also audited some larger state owned enterprises and their activities – maintenance and increase of the value of their assets. That was our second major consideration. And the third was that we had a role in preparing and suggesting personal decisions through making proposals. For example, for the state assets management agency we

made proposals for the members and the president of the supervisory board. For the state assets management companies we normally not just suggested but appointed the president of the supervisory board in the cases of the larger companies if not all companies. And also we had a say in the appointment of the independent auditors for the state assets management company. Sometimes felt a little bit heavy with this authorization to be so active in these personal decisions but finally the State Audit office could solve this heavy difficult task without any serious problem in the last half of decade.

Let's turn now to the experience of the State Audit Office. As regards the experiences concerned the State Audit Office regularly informed the Parliament of its findings. Yet there were many references to the privatization invert – even at the plenary sessions not just at commission sessions – but despite this the parliamentary control over the privatization was rather weak due to the very complicate political debates. However, special investigation comities often benefited from our reports. There were several in the last 14 or 15 years because it was heavy that politicians always suggested special investigation comity on a special deal. The State Audit Office focusing on regular audits meet some hundred proposals for privatization in order to correct procedure irregularities mainly like corruption risks, cases on malpractice, violation of accounting discipline, etc. Another group of irregularities was related with regular faults of the so called organizational operations in the case of organizations who dealt with privatization. It is the third group I mentioned are irregularities identified by State Audit Office in the very heavy process of the so called bank consolidation which was very closely attached to the privatization process. We made our proposals through our reports, however the implementation sometimes still late behind. Generally speaking about two sorts of our suggestions, recommendations, they received well and implemented but the rest was not considered seriously. So we have consequently been not very satisfied with this situation. We also initiated a few court procedures where we found that the corruption case were there. The number of these cases is about 110.

Putting together our experiences I dare to say that we contributed to the fairly successful process of the Hungarian privatization and the second point is that we could benefit from INTOSAI guidelines particularly in the last six years. Hungary is of course member of the working group on the privatization from the very beginning. I personally use to represent the country for the last couple of years in the work of the working group.

Now I would like to turn to my third subject area. That is the guidelines on the best practice for the audit of risk in public and private partnerships. There are also guidelines for this field. The guidelines have been also elaborated by the working group but these guidelines could not be taken as finished as yet. We are working on developing further the guidelines, correcting it on the basis of experiences gained by the member countries. The guidelines should be taken as an audit methodology which is the case in guidelines on the privatization. Here guidelines focus rather on the risk inherent in PPPs partnership – both to the state and to the State Audit Institutions. The risk areas facing the state are there. Clarity about partnership objectives – that is very important. Second risk area for which there are guidelines is the negotiation with appropriate partnership. Here I mention that 7 guidelines is for the risk especially and to draw attention to the danger which might become from the specialist – financial or legal advisors who are hired by the state and state's institutions. The risk here is that this specialist, advisors could not behave quite well. Their integrity might be questioned and secondly too much money is offered normally for them. So these are the main point here in the seven guidelines concerning the corruption. Of course there are direct references for the public employees as well who may be bribed in favor of company, for example in the procurement process or in concluding partnership agreement with a private company. So I draw your attention especially to the seven guidelines on corruption.

Other risky area is the state`s protection, the monitoring and also some risky area for the State Audit Institutions. In Hungary, the PPP is very popular method recently; perhaps it is too popular. The main areas of the PPP are the following motorway construction, prison building, and educational projects like hostels...

The estimated present value of the total PPP project in Hungary is some 611 billion florins. This equals to 2.4% of the GDP. This is of course total, cumulative figure. There is a rule in Hungary that the annual new PPP decisions could not be higher than the 2% of the expenditure total of the yearly budget. So it is actually a rule based type of the regulation. The annual new PPP decisions for the states equals to some 0.7-0.6%. It is far from being maximum 2% possibility. From this year on we change this rules from the expenditure total to the income total of the budget by saying that new PPP decisions made by the government can not exceed the 3% of the revenue total of the budget because the safe side is on the revenue side not the expenditure side.

Vladimir RADIĆ,
KPMG d.o.o.

TRANSPARENCY AT THE PUBLIC-PRIVATE INTERFACE

I am going to read something from the perspective of KPMG as an Audit Office and its experience considering transparency between the private and public sector. Maybe, it is not so connected with this subject which is planned for the period between 13h and 15.30h and which refers to financing of the political parties. I hope you will find something useful here.

It has been in use in our country during democratization of the public administration and the establishing of the control over state organs and institutions. Namely, it refers to a segment which task is the state financing and a need for transparency – we are talking about all those actions when the state funds are collected, distributed, spent, given...

The responsibility of authorities can be measured by their transparency. The Government is obligated to give clear, understandable and precise information to people who elected them, tax payers, to those who actually invest in the state.

Unfortunately, we are often witnesses of an inappropriate use of this term which gets a negative connotation in the pejorative context.

One prominent gentleman, Ian Bowl, the executive director of the International Federation of Accountants has defined three reasons why the citizens must be informed by the state.

The first reason is responsibility. The state does not spend its own money, but ours.

Conscientious running of the state policy means that the tax – payers are citizens authorized to get information about dealing with the state resources; about how capable the state really is to give its citizens what they really need; is it capable to endure the extern blows on its potentials; is it capable to deal with challenges such as the connec-

tion between current obligations and long-term trends (aging of the population as a global phenomenon).

The second reason is the running quality.

A Government like a corporation must have accurate information about its own financial potentials in order to track the state running realization.

Basically, there is no difference between the state and corporative management.

States all over the world transfer billions of dollars under excuse of development of social and macro – economic role of the state. If the procedure is ineffective, if there is no control and if the funds are invested improperly, the economy will be surely the main victim.

The third reason is democracy. The proper implementation of democracy demands that a citizen should have trust in politicians and, on that basis, participates in the political processes.

You get that trust when the citizens are informed which helps the citizens in modern democratic societies to make decisions.

Information about conscientious running of the state funds is often crucial when making an election decision.

The quality of the state management is improved by the transparency in the state finance. The citizens deserve something like that in democracy. That improves the fight against corruption and corruptive actions of the state administration.

I shall say something about the level of transparency in the public sector from the perspective of KPMG. Is the work of the state authorities (the Ministry of Finance, the Ministry of Economy, Tax Administration, Customs) handling with state funds or is the privatization process transparent enough? That must be analyzed by numerous teams of experts.

The most important thing is that the public control has begun to function lately. That is obvious. It is impossible to think about further state modernization, finishing of the reform process and the transition without it.

If there is any employee of the state administration here, I would like to apologize for this comment, but they generally have an irrational, even malicious tendency in handling big amounts of money. They are exposed to multiple control and supervision in Serbia nowadays.

A fact that the uncontrolled freedom even arrogance of the public sector is not possible nowadays must be accepted. That process can not be blocked.

I will mention three examples through which the auditors can see how much the transparency of the public sector has been improved.

Public procurements. We were witnesses of some serious problems which affects both the purchaser and the supplier. It has occurred in the beginning of the application of the Public Procurements Law. Procedures were unclear, complex, uncompleted. There have been made a lot of mistakes. Public procurements were canceled. Critics were common thing and they recommended that this Law should be canceled, because „the economy is blocked by it". It is absolutely „out" to talk about these critics nowadays. The order in this area has been established. It seams that there are less abuses. Public procurements are carried out without problems, more or less. I am talking about the public procurements in which the KPMG participates.

The most serious problem was a long and inexplicable delay of the beginning of work of the Commission for the rights protection of the supplier, as a control agency.

The second thing refers to the inexplicable and unclear explanations referring to the system of appraisal of so called Commission for choosing the best supplier.

If the appraisal of higher criteria was in question, there would be some very unusual explanations why something was selected instead of something else. Transparency is seriously endangered in those circumstances.

After some beginning problems and scandalous privatizations we entered a stable, organized and very transparent process.

The common remarks were given on a few privatization participants when speaking about local businessmen. We have to agree that the experiences of other countries in the region are similar. The biggest acquisitions have been done with multinational companies as buyers. They did not have any complaints on the procedure's transparency. They were more frequent. The remarks and critics were mainly directed to the preparations in the privatization process, above all to the bad documentation which should help the investor to make a decision. But then, we have got a problem with competency, not with transparency.

Privatization is about to end. That is an encouraging fact. However, I have to mention a critique to the Government because of the absence of efforts to implement the privatization on the public companies and big state systems. It makes us mistrustful regarding state efforts in consistent and transparent process of the reforms and transition.

The last thing from our experience is establishing of the Audit Office and a auditor function in the public sector.

Insisting in establishing the Audit Office in the public sector, (in positive way) has contributed to one new, higher – quality understanding of the auditor profession and understanding of the significance and value of the audit itself.

It would be decent to emphasize the importance of the work of the Serbian Government. I would specially like to emphasize people from the responsible departments who have created some law prerequisites to help the audit's functionality.

After 2001 the audit has stopped to be just an obligation by law for the public sector, fulfilling of the form, the work where only the auditor takes the benefit by a compensation.

Some public institutions had their property revised for the first time in spite of their long existence.

The auditors have shown the health condition of numerous factors in the public sector by their objective approach. The transparency of the financial results which were achieved in the public sector (thanks to the work of the auditors) has sometimes pointed out a need for an appliance of drastic and unpopular measures. Let us remember the closing of four big state banks. Eventually, it has shown a very bad management structure, in other words personnel structure in the public sector.

A fact that the reports have often been ignored certainly leaves a bad impression. There have not been any reactions on our results.

We have been making the same mistakes for years. There is the main difference between the public and the private sector. I think it is completely impossible for an owner or a representative of the Government or a company not to react when an auditor points out the existence of the risk or mistakes in a financial report of a company, a bank or an insurance company.

Selection of the auditor or the evaluator of the property or the capital of the public companies is based on the cheapest offer (economically the best offer) and that fact must be taken into consideration by the state. It brings us to the hiring of an auditor or a consultant with limited qualities and potentials.

You get an impression that an auditor has become a partner in a mutual work and that the public sector has no doubt about audit's effectiveness.

The Laws on the Conflict of Interest, the Rights and Obligations of the Officials on public functions, the Public Information and the Financing of the Political Parties have contributed to the transparency in the public sector in generall. It would be really rude not to mention the state organs and first of all The Anti Corruption Council which are in charge for the control and application of these regulations. The non – governmental sector and some other organizations have improved the transparency of the every day processes in this country by their persistent and constructive approach.

Serbia has understood the significance of the Latin word from the beginning of this text with a big delay comparing with the surrounding countries. That delay can not be justified by certain weaknesses and defects referring to persistent insisting in the full public insight in the state's procedures and processes. That is very important because of the fact (and it has been said earlier) that it is basically our money.

I shall be much shorter when talking about private sector, even though our experiences are much stronger. Introducing the international standard referring to financial reports (as an integral part of the national bookkeeping policy, 2003. a bank year, 2004. a corporation year) has influenced on improving of the transparency level of the financial reports in the public sector in Serbia.

The improvement of the international standards of the financial reports is completed rapidly and the transparency level is growing. The significance of the auditors is exactly in help we give in the implementation of these standards. It comes from our huge experience in this area.

I think that the potentials in this country have not been fully used. The examples of our engagement by the private or public sector to help them implement these standards are rare. We have been working for a few banks including the NBS.

The experience of the KPMG referring to the practice in the public and private sector is that this part is still full of problems referring to the proper implementation of the international standards. There are lots of reasons. Some of them are the lack of knowledge, misunderstanding of a need and a direct efficacy, misunderstanding of an auditor's function, unsatisfied improvement and organization of the financial market or the stock market, bad law harmonization. The Tax and Bookkeeping Laws have not been harmonized completely with the implementation of the international standards.

We should be aware that the proper implementation of the international standards is a big step forward, but not the only guarantee of

the transparency in the public and private sector. We all know for the well known scandals like „Enron", „WorldCom", „Parmalat", etc which have contributed the introducing of the Serbanes – Oxley Act firstly in America and afterwards in all European countries. The auditor's function has been taken more serious in order to protect so called stay holder.

In the end, what would be the conclusion? First of all, we need a consistent implementation of the existing pieces of legislation which makes a foundation of the transparency for both the public and the private sector. That is not enough. It is necessary to change and harmonize the regulations with the practice of the developed countries of the Europe and the world.

The remarks that some changes could lead to the legal insecurity simply do not stand. The society is changing fast nowadays and it must be followed by the regulations which have the same pace.

Finally, and maybe the most important is improving of the education, in other words those facts from which the transparency in the public and private sector depends on. We have a strong impression that the state and private sector in Serbia are willing to save particularly on the staff education what is really irrational. Referring to this matter, we are unusually rational. In the KPMG which has got big investments in employees (measured in hundreds of thousands of euros) we are aware that the budget, plans and realization are loaded with these investments.

But, the benefit is very big. It seams that the education is the biggest problem of the transparency in Serbia nowadays.

PhD *Milić MILOVANOVIĆ*,
Professor at the Belgrade Faculty of Economy
The Anti-Corruption Council of The Government of Serbia

NATIONAL INVESTMENT PLAN AS A CAUSE OF COLLAPSE OF THE BUDGETARY SYSTEM

I would like to add to what has just been said. I am also fascinated by the fact that we do not have an Audit Institution on the state level. I can not believe that seven years after the democratic changes in Serbia, this institution which is formally, and legally established, has not yet become operative.

I have spoken openly in favor of this institution on many occasions, and I have no words to express my disbelief, bearing in mind that from the year 2000 political life in Serbia was dominated by the so called democratic parties. One Democratic Party prides in its progressiveness, and Western orientation, i.e. European Union. We have seen, however, that a Central Audit Institution holds an important position in the European Union and in the West in general. When talking about the civilized world, Serbia is, consequently, an exception, not only in Europe, but worldwide as well, since it has no such institution. It is incredible that one Democratic Party, a pro European one, and on power since the democratic changes till the end of 2003, failed to establish this institution.

I also do not understand that the other Democratic Party, with a more national orientation, and trying to keep some traditional values in our society, and headed by a lawyer engaged in Constitutional Law, and probably acquainted with the Constitutions of the former Serbia and Yugoslavia, that even this Party was not interested in the establishment of the Central Audit Institution. Moreover, all institutions, both in the Kingdom of Yugoslavia, and Serbia in the 19the century had its independent Audit Institution.

A situation like this provokes a great puzzle, even though we should not be surprised to that extent, taking into account the political unreadyness, that is the lack of the political will to establish the control of the public finances.

We have been discussing the need for the establishment of this institution for two days, mentioning its advantages, its tasks, the pitfalls in the way of its establishment, i.e. the elements that should be taken care of constantly. Therefore, I have to point out that after the presentation of Mr. Hokesvort I have become even more pessimist. Yesterday he spoke of the principles of the healthy budgetary system. He pointed out that each budgetary system, aiming to be healthy, has to be based on three principles. Unfortunately, not one of these principles is met in our budgetary system. Our budgetary system has serious weaknesses, and it seams to me that in such a system, which lacks in principles, referred to by Mr. Hokesvort, that in such a system the existence of a Central Audit Institution makes no sense.

Namely, the Central Audit Institution may perform its task properly only if the target of the control is known. In our reality, we even do not know the overall amount of the state budget. The budget was breached, we do not know where one budgetary year ends, and the other begins. Mr. Djelic spoke of that yesterday. I would just like to add that upon the implementation of the National Investment Plan, we are no longer capable of knowing the budget of the country. The funds can be transferred from one year to another. If a project was financed in the last year, it can continue to receive the last year's budgetary funds in the next year. Also, if a different project which in a lesser degree began its realization in the previous year, it will continue to receive the funds from a new budget in the next year. Therefore, we are completely confused about the budget of our country, the end of one budgetary year, i.e. when we draw the line saying the budget had surplus or deficit. At the moment we do not know if the last year's budget achieved surplus or deficit. Even without the problem Mr. Djelic spoke about, without the fact that the funds obtained trough privatization procedure are aggregated to the budget without being marked, and thus the false impression of a surplus is created, while there is an actual deficit. Namely, we still do not know the amount of the funds spent on the National Investment Plan in the last year. Some extremely contradictory data regarding this matter appeared in the public, and we can only speculate on the actual expenditure of the funds.

Hence, our budget was breached, and one of the first tasks of the new Government is to reform the budget. Mr. Djelic was right to point out to this, and we shall remind him of his words, when he becomes a member of the Government.

I expect the new Government to either annul the National Investment Plan, or to include it completely into the budgetary system, because the present situation is unsustainable.

I have discussed the National Investment Plan before, and I do not want to bother you with repeating some of my estimations, particularly that we are getting near to the end of this conference. I must, however, point out that the very existence of the National Investment Plan is an obstacle to the achievement of the principles of the healthy budgetary system.

The principles of the healthy budgetary system would never be achieved, if we continue with the financing that we have nowadays.

Maybe I should make few details regarding the National Investment Plan, in order to be clearer.

For instance, Mr. Hokesvort said that each annual budget must be a part of the medium term planning system. I could not agree more, and I may add that some similar elements already existed in our practice. Each year, the Government, at the suggestion of the Ministry of Finance, adopted the Memorandum on Budget and Economic Policy, not only for the next year, but also for the two years ahead. This system ensured the stability of the fiscal policy for several years ahead, so that the industrial subjects could know what to expect in the next year and what in the next two years.

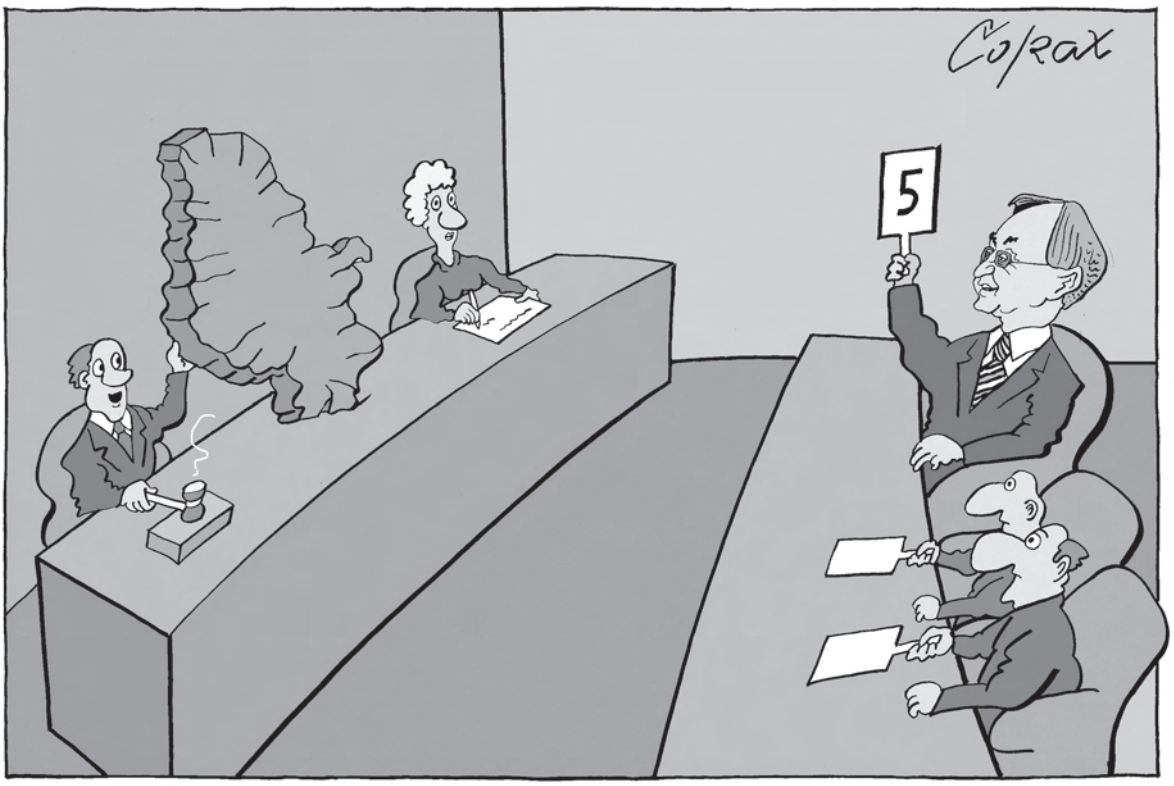
In May 2006 the Memorandum on Budget was published without mentioning the adoption of the National Investment Plan. In the next month, however, the Minister of Finance, who wrote up the Memorandum on Budget, came up with the idea to create the National Investment Plan and spend EUR 700 million in the same and the next year. Completely contrary to the medium term plan and the system in which each annual budget should be a part of the medium term plan. We are facing a completely new situation: a major growth of the state investments, and, generally, a growth of the public expenditures, contrary to the Memorandum which said that there would be a reduction of the public expenditure participation in the GDP.

Not only that this was done, but by the end of the year changes were made in the Law on Budgetary System. Namely, the Law on Budgetary System envisaged that each year an annual budget is to be adopted, but with the National Investment Plan the system of continuous budgeting was introduced, and this had to be included in the Law. However, this fact speaks of complete political arbitrary decision making, willing to amend the systemic laws in order to achieve its particular interest. This creates an uncertainty in a political, but above all, in an economic sphere, and this increased uncertainty increases the growth of corruption.

The very essence of the National Investment Plan has series of shortcomings, and according to our opinion facilitates the corruption significantly. I would, however, like to point out here that the instability of the economic system and the economic opportunities in the country also contributes to the growth of the corruption. Particularly that the individual subjects are no longer able to have a long-term insight, and to plan their activities ahead. Instead they are looking to achieve a certain profit in a short-term period, and corruption is the way they use the most.

We have an important task ahead of us. It does not only involve the establishment of the Central Audit Institution, but putting it to work as well, and the establishment of the administration that would facilitate the work of this institution. At the same time, we have to make serious efforts in order to make budgetary system transparent and comparable to the ones existing in the OEBS countries.

In the end, I could, maybe, finish with a personal remark, because in time I have become a pessimist. When I began my carrier as an economist, my country was an associated member of the OEBS. Not only that, we were the only socialist country which was the associated member of the European Economic Community. Today, unfortunately, it looks like chances of admission to the EU, or for a membership in the OEBS are null. It appears that we have a long way ahead of us, which is getting more and more prolonged, to become a part of the international integration, and one of the major obstacles on this road is a high lever of corruption in the country.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REPORTS / INITIATIVES

REPORT ON THE HORGOŠ-POŽEGA HIGHWAY CONCESSION

The 1996 Republic Area Plan („Official Gazette of the Republic of Serbia No. 13/96), foresees the building of the E–763 highway from Belgrade to the South Adriatic. It was judged at the time that this highway route has a priority strategic significance for connecting Serbia with Montenegro and for the enhancement of the integration processes in the Federal Republic of Yugoslavia. However, no preliminary design solution had been made for this highway until the disintegration of the Federal Republic of Yugoslavia and its successor, the State Community of Serbia and Montenegro.

A highway that is very important for the European Union, the so-called Corridor 10, connecting Saltsburg and Salonika, via Ljubljana, Zagreb, Belgrade and Skopje, was to be built over the territory of Serbia. Three branches of this Corridor, which are considered as an integral part of the highway, were foreseen, i.e: Graz-Maribor-Zagreb, Budapest-Segedin-Subotica-Novi Sad-Belgrade and Nis-Sophia. The European Union, and particularly its member state Greece insisted on the completion of this Corridor on a number of occasions, particularly before the Olympic Games in Athens in 2004. Corridor 10 was placed on the European Priority List by a decision of the Working Group of the European Commission for Transport from March 2005.

The parts of Corridor 10 through our country have not been finished yet between Leskovac and the Macedonian border, nor have its branches, i.e: the highway between Nis and the Bulgarian border, the left highway lane between Horgosh and Novi Sad and the parts of the highway Novi Sad – Belgrade (the completion foreseen by the end of 2008).

It was foreseen by the National Investment Plan (NIP) that 8 million euros be invested in 2006 for the building of the highways Leskovac-Presevo and Nis-Dimitrovgrad, which was approximately

sufficient for 2 kilometers of the highway. By the Government Decision of 26 July 2007 it was foreseen that in this year 310 million dinars be invested for the building of the mentioned highways, which is 4 million euros less (at the same time 329 million dinars was foreseen for construction of ski tracks).

Instead of funding the building of these highways by assigning budget funds or taking loans from international financial institutions, the Government decided to build a new highway route from Belgrade to Pozega, and by granting a concession to a foreign investor (potential domestic investors were excluded by the Decision on Granting the Concession, Official Gazette of the Republic of Serbia No. 80/05, according to which the Concessionaire must have an annual turnover of 4 billion euros minimum, which is nearly one fifth of the GNP of Serbia).

This highway route is connected in an unusual way to the Horgosh-Belgrade branch of Corridor 10. It is stated in the Proposal for Granting Concession sent by the Ministry for Capital Investments to the Government how the highway to Pozega „is logically connected to the Horgosh-Belgrade section (the northern branch of Corridor 10) making thus a whole which would be the subject of the concession". Besides, it is stated in the Proposal that there is „an interest of the Republic of Serbia to build the highway from Belgrade to Pozega". But this section is characterized by high investment costs, so that, with the maximum concession period of 30 years, the potential investor would not be able to make a satisfactory returns rate. In other words, the small traffic frequency on this highway, the toll collection, with a minimum concession fee to the state, could not cover the required investments and an adequate returns rate. Therefore, it was proposed that this route be connected with a much more frequent branch of Corridor 10.

The Proposal for Granting the Concession was not made in accordance with the Concession Law (Official Gazette of the Republic of Serbia No. 55/03) in at least two aspects. Article 8 of the said Law requires the competent Ministry to prepare a proposal „on the basis of economic, financial, social and other indicators". Out of all these aspects the Proposal states only that „the delay of the building may have negative consequences both for the entire economic development and for the integration into the European Community"(?). As regards the Belgrade-Pozega route, it is said that „the traffic research related to traffic analysis and prognoses so far suggest the need for the building of the subject highway". Then it is stated in brackets that a load in-

crease has been noticed, that „there are frequent bottleneck situations", and a great number of tragic traffic accidents.

Another aspect where the Proposal departs from the Law is the attitude of the Proposal maker that the „the building of the highway is to be implemented by granting a BOT concession". The abbreviation BOT stands for the English words *build-operate-transfer* (according to the Law *izgradi-koristi-predaj /build-operate-transfer/*) and it means that the investor shall build, use over the specified period of time and then transfer it to the ownership of the Republic of Serbia (Article 3). It is clear from the very Proposal that this concession model cannot be applied in the particular case, as the most part of the subject of the concession has already been built: Novi Sad – Belgrade and the right lane of the Horgosh – Novi Sad highway. In the first case the Concessionaire has no obligation, not even to maintain the highway, until 2009, but in spite of that they may collect a toll. The Proposal maker explains this solution by the need for the funding of the Belgrade – Pozega route. But if the building of that section is funded by the collection of the toll on the already built highway, then we cannot say that it is a BOT concession, because the Concessionaire builds the highway by exploiting the subject of the concession.

Besides, it is worth mentioning that the Proposal contains the information that the budget for the completion of the Horgosh – Novi Sad section is short by 138 million euros. At the same time the state authorities of Vojvodina have presented information to the public that an amount of approximately 40 million euros is collected on this highway route per annum, which means that the completion of this branch of Corridor 10 can be easily funded from the collected toll.

The Concessionaire is given a public good – a highway – to operate and collect toll, but they are not obliged to pay back the loans obtained for the building of this section of the highway (the bridge near Beska, the ring-road and the highway Novi Sad – Belgrade), nor a compensation for the completed works, which have not been paid for.

Government's Authorization to Conclude Concession Agreement

According to Article 16, Paragraph 3, of the Law on Government (Official Gazette of the Republic of Serbia No. 55/05), the mandate of the Government ends with the termination of the mandate of the National Assembly, which is in accordance with Article 89 of the Constitution.

According to Article 17, Paragraph 1, of the same Law, the Government whose mandate has ended may perform only the current duties.

According to the Law on Government, the current duties of the Government are only those duties which do not require bringing of any permanent decisions, but constitute only the duties of representing the Republic of Serbia as a legal entity, exercising the rights and carrying out the obligations of the Republic of Serbia as the founder of public companies, institutions and other organizations (Article 4 of the Law), as well as the duties related to the supervision of the work of the state administration (Article 8 of the Law). All other tasks, such as the divestiture of the property of the Republic of Serbia, making proposals to the National Assembly for the adoption of laws, adoption of regulations, the appointment of state administration officials, and similar duties, are duties that cannot be performed by a government whose mandate has ended.

The National Assembly was dissolved on 10 November 2006. Since that date, i.e. by the termination of the mandate of the National Assembly, the mandate of the Government has ended as well, and since that date the Government has had the right only to perform the current duties and it has not had the right to undertake any actions constituting the divestiture of the property of the Republic of Serbia.

On 3 November 2006 the Government brought the decision on the selection of the Concessionaire for the funding, designing, operation and maintenance of the highway section from Horgosh to Pozega. As foreseen by the mentioned Decision, on 9 November, by a special decision, the Government established a commission to conduct the negotiations with the Concessionaire. However, this Commission is authorized only to conduct negotiations because, according to Article 23 of the Concession Law, only the Government has the power to conclude a concession agreement in the name and on behalf of the Republic of Serbia.

The Agreement between the parties was concluded when the contractual parties agreed on the essential components of the Agreement, in the light of Article 26 of the Law of Obligations (Official Gazette of the FRY No. 31/93). The Concession Agreement is concluded in writing (Article 21 of the Concession Law) and it is considered concluded at the moment when signed by the Concessionaire and the Concessioning Authority. The Government concluded the Agreement on 30 March 2007.

We find that the conclusion of a concession agreement is not a current task of the Government, and that a government whose mandate

has ended is not authorized to conclude agreements granting the right of the use of a natural good in general use.

Conclusion

The example of granting the concession for funding, designing, building, operation and maintenance of the Horgosh – Pozega Highway is very significant as regards the struggle against corruption. It indicates that politicians and the executive power use public goods for individual or party interests. In this case, these interests are primarily reflected in the fact that public roads are built to the constituency of the line minister, so that he can exercise his political influence. The final destination of the route of the foreseen highway does not have a major economic, financial, social or strategic significance, as regards the general interest of the Republic. On the other hand, the completion of Corridor 10, together with its branches, is a true strategic priority of the country. Most of the cargo and passenger transport and traffic are carried by this Corridor, and it is at the same time the shortest connection between the European Union and its two member states, as well as the Near East countries. If joining the European Union is really an objective of Serbia, all the roads constituting Corridor 10 must be built within the shortest possible time, as the EU Commission has pointed to it as one of its priorities.

The Anti-Corruption Council finds that the bringing of the decision on the concession for funding, designing, building, operation and maintenance of the Horgosh – Pozega Highway, as well as the exceeding of the authority of the technical Government when concluding the Concession Agreement, constitute an explicit example of political corruption, which will be inevitably negatively reflected in all other aspects of society.

Belgrade,
September 3, 2007

Yours faithfully,
President
Mrs. Verica Barać

ПИСМО САВЕТА ВЛАДИ РЕПУБЛИКЕ СРБИЈЕ У ВЕЗИ СА ПРЕУЗИМАЊЕМ ПРЕДУЗЕЋА „Ц –МАРКЕТ“ И АУТЕНТИЧАН ТЕКСТ МЕМОРАНДУМА О РАЗУМЕВАЊУ, КОЈИ ПРЕДСТАВЉА КАРТЕЛСКИ СПОРАЗУМ О ИЗБЕГАВАЊУ КОНКУРЕНЦИЈЕ

THE GOVERNMENT OF THE REPUBLIC OF SERBIA
– Prime Minister Vojislav Koštunica –

B e l g r a d e

Dear Sir,

The Anti-Corruption Council has received a number of complaints with comprehensive documentation related to the takeover of „C-market“ a.d. in 2005 with claims about illegal agreements concerning the takeover of the shares from small shareholders of this enterprise between the potential buyers „Delta M“ and „Laderna B.P.“ and the Director of „C-market“, on the initiative of the Prime Minister of the Republic of Serbia, and in the organization of Mr. Danko Djunic. Enclosed are the complaints received by the Council, as well as a Memorandum of Understanding, signed between the mentioned parties. The persons who sent the complaints claim that the signing of the Memorandum caused the other tenderers to withdraw from participating in the Tender, and after that, 77% of the „C-market“ shares were bought by the Memorandum signatories at a previously-fixed price, allegedly four times lower than the estimated value.

As the Anti-Corruption Council is preparing a report on the takeover of „C-market“, please inform us whether the documentation we have received is authentic or not.

Belgrade,
August 20, 2007

Yours faithfully,
President
Mrs. Verica Barać

Memorandum of Understanding

Memorandum

At the initiative of the Prime Minister of the Republic of Serbia and at the invitation of Mr. Danko Đunić, on August 19th 2005 the following parties met at the business premises of the company EKI Investment d.o.o., located in 16 Kralja Milana St., in Belgrade:

1. Delta M d.o.o., represented by Mr Miroslav Mišković;

2a. C Market AD, represented by Mr Slobodan Radulović;

2b. Laderna B.V., represented by Mr Milan Beko;

In order to boost national economy and ensure efficient national market as a whole, especially financial market, the parties have signed the following:

Memorandum of Understanding

having thus agreed to the following common principles:

1. Both parties shall put an end to any hostile activities related to single takeover of the company C Market;
2. The Companies Delta M and Laderna B.V. shall jointly participate in the privatization process of the company C Market (hereinafter referred to as Project), because of financial and business restructuring as well as preservation of C Market brand;
3. The equity capital in the Project has been defined for the period of 2 years. The value of the Project presumes all necessary investments to be made (purchase of minority shareholders' shares, necessary recapitalization due to financial and business restructuring, as well as purchase of state shares), in the following ratio:

    a. 60% share of the company Laderna B.V.,
    b. 40% share of the company Delta M, i.e. other related entity

4. The Project shall be realized as a combination of takeover bid and recapitalization, in the following manner:

    a. Takeover of the company C Market from the company Primer C under the same conditions the company Delta M has already offered to minority shareholders. The company Delta M shall

become the owner of the company Primer C as per agreed equity ratio, according to Article 3;

b. The recapitalization of the company C Market to be done by the company Delmot S.A., joint legal entity Delta M and Laderna B.V., as per agreed equity ratio defined in Article 3, and in accordance with the Study on Restructuring of C Market.

5. Upon the expiry of the agreed period of 2 years, and for the ensuing period of 6 months:

   a. Company Delta M shall preserve the right to Call Option over the company Laderna B.V., which presumes the right to purchase the shares of the companies Delmot S.A. and Primer C owned by the company Laderna B.V. at the previously agreed price.

   b. Company Laderna B.V. shall have the right to Put Option over the company Delta M , which implies the right to sell the shares of the companies Delmot S.A. and Primer C it ownes at the previously agreed price. This also presumes that in this case the company Delta M is obliged to purchase the above-mentioned shares from the company Laderna B.V. accordingly.

   c. The pattern defining the shares price in case of Put and Call Options shall be duly defined and based on the market price of the company C Market according to the prevailing international practice which is applied in such transactions and on the basis of weighted average of EBITDA multiplicator and revenue of the company C Market at the moment of realization of Put or Call Option;

   d. Put and Call Options shall be ensured by depositing shares of the companies Delmot S.A. and Primer C in appropriate manner, with the joint trustee;

   e. Upon they expiry of the period of 6 months, provided that neither Put nor Call Option has been used, the parties preserve the right to initiate sale of shares of the company C Market in the companies Delmot S.A. and Primer C to the third party. It has been agreed that a sales mode used in this case shall be in accordance with the international practice of engaging an investment consultant in the sales process. Furthermore, the parties have agreed to adhere to the principles Tag-Along and Drag-Along;

Memorandum of Understanding

f. The parties have agreed not to purchase the shares of the company C Market directly, or through other related legal entities, or by any other means but those defined in Article 3.

6. The signatories to the Agreement shall each engage renowned foreign law offices to draw an Act on Legal Relations resulting from Agreement of Understanding. With that regard:

a. All contracts shall be made in English
b. The contracts shall be subject to Austrian Law
c. The language of the arbitration shall be English, whereas the place of arbitration shall be Vienna, Austria

7. During the process of contract draft, both parties Delta M and Laderna B.V. preserve the right to change the companies they have each chosen to represent their interests and rights accordingly, while abiding by the principles defined in this Memorandum.

8. The contracting parties have agreed that the company EKI Investment shall provide expertise in realization of this Agreement.

9. This Agreement has been made in 2 (two) identical copies, one for each Party.

Signatures:

Delta M d.o.o.	Laderna B.V.	C Market a.d.
Milorad Mišković	Milan Beko	Slobodan Radulović

Witnesses thereof:

EKI Investment d.o.o.
Danko Đunić

August 19th, 2005
Belgrade

REPORT ON THE COMPANY „C MARKET“

The privatization of the Company „C Market“ brought to light numerous drawbacks of our political, legal and economic system, which contribute heavily to the general growth of corruption in the country.

According to data known to the public thus far, one could reach a conclusion that the participants in the privatization procedure of the „C Market“, as well as the other interested parties, performed various violations of the law. These infringements pushed a very successful company, the proprietor of the considerable property, into the economic downfall, and led to its practical disappearance from the market.

We hope that the Court shall determine the whole truth on this subject. It is up to the Anti-Corruption Council, however, to alert the Government to possible causes and consequences of corruption which this case clearly implies, and which have widespread significance, and could definitely not be pinned on the privatization of the „C Market“ solely.

Above all, one notices the fact that the socialist Director, who was the Head of the company in which there was little difference in the span of salaries, became the major owner of the company's capital. This capital, according to the estimates made by the Director himself, was worth several hundred million euros. The logical assumption would be that the Director probably did not pay the full market price for his share in the company's capital. Regardless of the possible abuse of his respective position, fraud or any other violation of the law, it should be pointed out that this is not an isolated case.

It is merely an example of consequences derived from the application of the travesty of the Law on Ownership Transformation from 1997 („The Official Gazette of the Federal Republic of Yugoslavia“ number 29/97), which practically secured privileged position of the Managing Directors in the privatization procedure. Surely the most

important privilege given to the Managing Directors was the fact that, even as owners of the minority share packages of the company, they succeeded in wining the dominant position in the company. By means of blackmails, falsified financial statements, connections to the judiciary and executive authorities, threats of dismissal against the workers-shareholders, and other forms of pressure as well, they expanded their ownership share. The documentation regarding the Company „C Market" gathered by the Council clearly points out to this direction. The process of the privatization, which by the end of the nineties and after the year 2000 in Serbia often favored the Managing Directors, led to a significant accumulation of the capital in the hands of individuals at times of a general poverty. Serbia became a country of penniless population and wealthy individuals. The fact that Serbia has four representatives among the hundred richest people in the East Europe, while Slovenia with almost five times larger income per capita has none, can be taken as illustration.

These altered economic and social surroundings were the setting in which Serbia adopted the new Law on Privatization in 2001 („The Official Gazette of the Republic of Serbia" number 38/01). Pursuant to this Law a main prerequisite for the purchase of the socially owned and the state capital was to hold the accumulated capital. One of the consequences of this Law is that the richest people, who acquired their capital in the period of sanctions and heavily controlled privatization procedure by the end of the nineties, continue to be in charge of the remaining privatization procedures nowadays as well. They are the first in line, say, during the privatization procedure of the oldest Mineral Water Plant, or once leading commercial chain of Department Stores, and purchase of the arable land, or in the case of the battle over the „C Market's „ownership.

The fact that an individual holds the wealth estimated at least 6% of the GDP, has not only economic, but a political significance as well. If this individual expresses interest in the privatization of a certain company, political circles instead of staying indifferent, would, according to the experiences so far, strive to indulge him. The case of the privatization of the „C Market" once again confirmed this unwritten rule, and this fact did not go unnoticed in public, since the politicians openly favored the „local buyer" in their respective statements, and courts passed bias rulings which hardly had any sound basis in the effective legislation.

The symbiosis between the political and economic power in the mentioned case is further strengthened by the standpoint of politicians

that the creation of the monopoly in possession of the local entities is far more favorable then allowing foreign entities to engage themselves in the retail business in Serbia. This attitude has been justified by the appeal to the national interest. The public, moreover, has been left in dark on the answer –whose interest that serves, whose interest has been declared the national interest? The political decision to create a trade monopoly, by all means, does not favor the interest of the consumers, or the manufacturers. It is well known that the competition among trade companies is always more favorable then the monopoly, both for the consumers, and manufacturers. The monopoly imposes higher prices on the consumers, while it pays lower prices to the suppliers, and they both incur losses in comparison to the competitive conditions. Only the newly established monopoly profits from this. Why were the interests of a company in a possession of one man declared the national interest, against the interests of millions of consumers and manufacturers?

The acquisition of the „C Market" by the retail network owned by the Company „Delta", led to the creation of the company that dominates the market, since, according to the words of one of the participants of this acquisition, this company now covers more then 60% of the legal retail market. This percentage by far breaches the limitation that the Law on Protection of Competition („The Official Gazette of the Republic of Serbia" number 79/2005) envisages as the limit for declaring that a company has the dominant position on the market (according to the Article 16 the limit is 40%). The establishment of the dominant company originates conditions for the abuse of the market position, or to put it bluntly, conditions for monopolistic behavior.

Several sources in the Council's documentation indicate that the meeting where the truce between the opposite parties was to be made, and the elements of the purchase agreement defined, including the quantity and the price of the C Market' shares was held under the sponsorship of certain members of the Government who were, at the same time, leaders of the ruling parties (Appendix 1: Memorandum of Understanding). According to the Director of the „C Market", who is now on the run, one meeting was held at the office of the Minister of Interior, where he was promised that „the police would stop all investigations of the „C Market" during the process of its privatization". (Appendix 2: Letter of Mr. Slobodan Radulovic forwarded to the Anti-Corruption Council). If these statements should prove correct, it would indicate serious meddling of the authorities into the economic flow.

It would seem reasonable to raise a question regarding the jurisdiction of the Minister of Interior, on account of which he expressed the interest in the privatization procedure of this company. Or, if certain individuals were under suspicion, how was it possible to postpone (stop) the investigation on account of the privatization procedure? When politicians show interest in the outcome of the negotiations of businessmen on ownership rights, then it is most often the case of corruption. National and international experiences clearly point out to this, since almost always the interest in business transactions is being expressed by politicians who themselves, or trough the parties they lead, expect material gain.

The fact that is even more disturbing, however, is that the deal was initiated and determined with the intention to harm free market principles by elimination of competition, to divide the market and fix the selling price of the shares. All these actions are forbidden by the Article 7 of the Law on Protection of Competition, which refers to all such agreements as null and void. Taking into consideration that Ministers, the Secretary-General of the Government of Serbia, and the Prime Minister are mentioned as initiators and indirect participants of this Agreement, it seems appropriate to form an interdepartmental Working Group that would gather all relevant facts regarding this case. The gathered data should be forwarded to the Commission for Protection of Competition, which should, ex officio, reach a decision comprising the obligatory measures to be taken by the immediate parties to the Agreement (pursuant to Articles 8 and 57 of the Law).

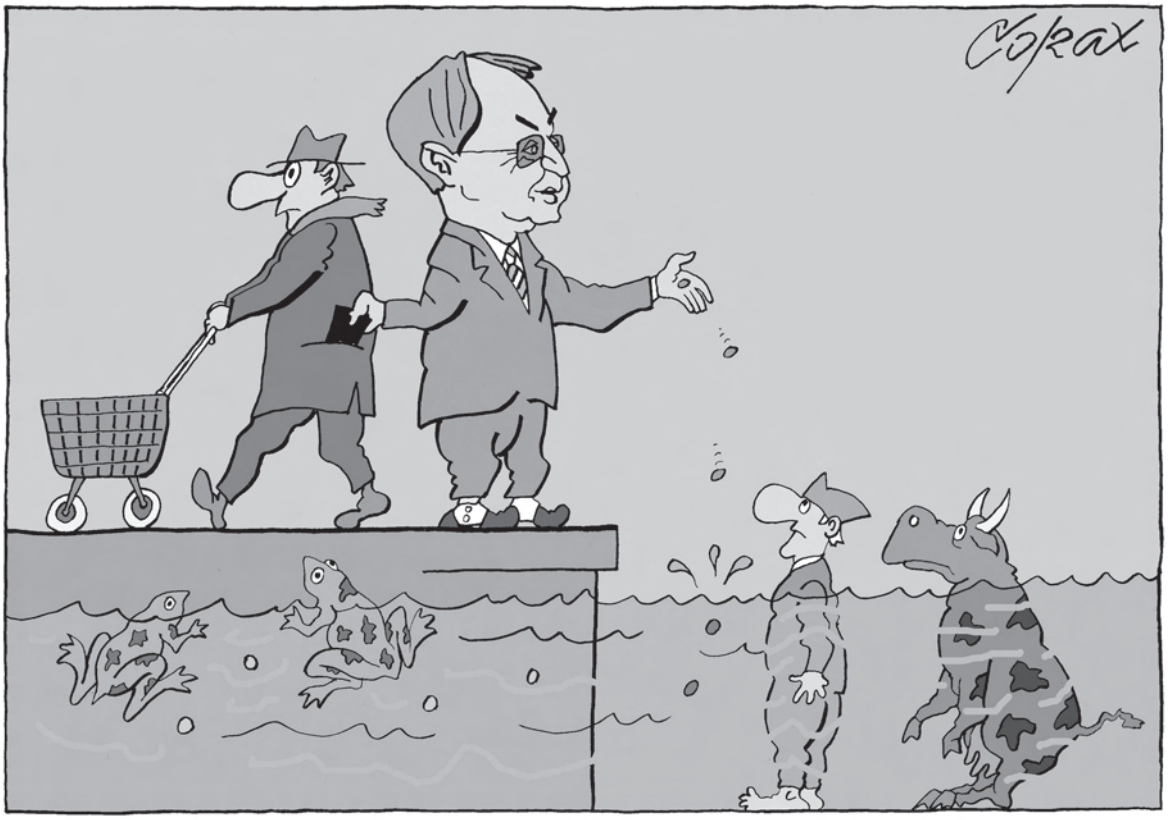
Our legislation does not envisage any material or criminal responsibility of physical persons who take part in the agreements that harm free market principles. Legislation of modern countries, nevertheless, regards all agreements on prices, prevention, restriction or distortion of the competition, or the division of the market as serious violations of the competitive conditions. Severe fines and imprisonment are prescribed for those who participate in such agreements, as well as for those who initiate them. The first Antitrust Law, adopted in the USA back in 1890 is still in effect, and envisages an imprisonment in the duration of three years, together with a fine. The French Corporate Law envisages the imprisonment for four years and EUR 75,000 fine. The English Enterprise Act envisages the imprisonment up to five years and unlimited fine, and the Company Managers could be banned from performing executive duties in the duration of fifteen years. The Anti-Corruption Council deems that the Law on Protection of Competition should be thoroughly examined and harmonized with the provisions in

effect in the European Union, especially with regard to the responsibility of the physical persons.

The Member States of the European Union regard the maintaining of the healthy market competition so highly that they incorporated these principles into the Constitutional Treaty of the Union. In connection to this, Articles 81 and 82 of this Treaty are very important for they define the common rules of competition. The European Union Council's Resolution of 16 December 2002 requires that all Member States have to incorporate the European rules of competition into their respective legislation. Also, all relevant authorities dealing with the protection of competition, including the courts, have to be vested with power to enforce the European rules directly. The legislation of the respective Member States, moreover, is not in any way impeded to prescribe even more harsh rules than those envisaged by the Union. The implementation of the European rules in our country requires not only the adoption of the modern Law on Protection of Competition, but the change of series of other laws, as well as their full observance. The Anti-Corruption Council, therefore, recommends the Government to commence the amendment of the relevant legislation as soon as possible, and to request its respective members to act according to the European principles. Being the highest executive authority, the Government must champion the implementation of the rules of the civilized society, serving as an example to other authorities. More precisely, and in connection with the privatization of the Company „C Market", the Council deems that aside from determining all facts and informing the public and the competent authorities accordingly, the Government has to determine the political responsibility of persons involved in actions, which, pursuant to the prevailing regulations are currently not liable to punishments, but differ from the European rules of protection of competition on the market.

Belgrade,
October 1, 2007

Yours faithfully,
President
Mrs. Verica Barać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COMMENTS ON THE LAW ON PROTECTION OF COMPETITION AND PROPOSED AMENDMENTS

The Law on protection of competition (Offical gazette of The Republic of Serbia No. 79/05) is the basic anti-monopoly act in our country. It is to regulate the business operations of monopolies, and to prevent the abuse of a monopolistic position in the market. This Law is also to establish criteria for mergers of companies so that their fusion would not create new monopolies or companies that would dominate the market. The importance of this Law cannot be overestimated. It is already an integral part of a well-organized market economy. The first anti-monopoly law was adopted in the USA as early as 1890 and is still in force. The European countries also developed their anti-monopoly legislation in the last century and, because of the importance paid to the struggle against monopoly, these provisions have been included in the Treaty Establishing the European Community. Especially significant in this Treaty are Articles 81 and 82 (the consolidated version from Nice). According to the EU Council Regulation No. 1/2003, all the member states must incorporate these provisions into their national legislations and enable the courts to apply these Articles directly and fully. Therefore, if our country intends to become a member of the European Club, it will have to elaborate its anti-monopoly legislation in accordance with the rules applied in it and which have been made explicit in the EU Commission Directives (2001/C 3/02).

Anti-monopoly laws are especially important in countries which are in transition from the planned economy to the market economy. The socialist doctrine of economic development put at the centre the increase of industrial production. It was believed that from the technological point of view the existence of only one producer in each industry was the most efficient. The monopoly problem did not exist at the time, because the prices were mainly state controlled. The transition

to market-controlled prices and privatization have created powerful monopolies in private hands. As each private company has the aim to make a maximum profit, these producers raise the prices and abuse their monopolistic position in another way.

This process has been intensified in our country for two reasons: the disintegration of the Yugoslav market resulted in the establishment of monopolies even in those industries where there used to be some competition and, on the other hand, the period of wars and sanctions resulted in a big concentration of wealth in the hands of few owners. This capital is now legalized and further concentrated by the creation of new monopolies. In this process the new tycoons will use any means to realize their goals, primarily by funding political parties and bribing state officials. This is the reason why combating monopoly is a very important element of the struggle against corruption in our country.

The Law on Protection of Competition, which was adopted in September 2005, does not meet the aims of an anti-monopoly law. It cannot ensure efficient combating of the existing monopolies, nor can it prevent the creation of new monopolies, which has already been proved in practice by the acquisition of C-market by the trading network controlled by Delta Holding, contrary to the opinion expressed by the Commission for Protection of Competition. The Government has prepared a proposal for changes and amendments to the Law (it is not clear whether it has proposed the adoption of a new law) and submitted it to the Council to give its opinion and proposals. Having studied the wording of the Law and its amendments, the Council has taken the following positions.

1. Subject and aim

The subject and aim of the Law have not been well defined. If these two factors are not clear to the drafter of the Law, one cannot expect a good law that will render good results through its application. It is stated in Article 1, which defines the subject and aim of the Law, that it „regulates the protection of competition in the market in order to provide identical conditions for the undertakings in the market, and with the aim to improve economic efficiency, and accomplish economic welfare for all the society, and particularly for the consumers...“This paragraph contains imprecise statements and even contradictions. Namely, the aim of the Law should be the protection of competition as one of the processes which renders many benefits for society, and

not the protection of the existing competitors (identical conditions for undertakings).

According to the Law, identical conditions for undertakings are important to stimulate economic efficiency. However, economic efficiency in modern anti-monopoly acts is a synonym for abandoning anti-monopoly measures for a short period of time, so that the producers would offer lower prices to the consumers by reducing the production and trade costs (Article 82, Paragraph 3 of the Treaty Establishing the European Community). The argument for economic efficiency is used as an exemption from the application of the general rule on the prohibition of agreements and associations of competitors. Thus our Law promotes an exemption to the level of a general principle.

Furthermore, the Law points out as its aim „accomplishing economic welfare for all society, and particularly for the consumers...". These two aims are often contradictory. When you speak about the economic welfare of all society, you also think of the welfare of the monopolist, but the aim of an anti-monopoly law is reducing his welfare. The application of the Law should lead to the lowering of monopoly rents, which, certainly, is not in the interest of monopolies. For this reason, anti-monopoly rules put at the centre the interests of the consumers whose welfare is improved by the lowering of prices, as well as the interests of the producers who are forced to sell goods to the buyer who, through his dominant position in the market, manages to ensure prices which are lower than those of competitors (these prices will be increased by anti-monopoly measures). In both cases, the position of one group is improved and the position of the other group is worsened. As the welfare of individuals cannot be compared, the welfare of society as a whole cannot be measured by the deduction of the losses from the profit of individuals.

2. Relevant market

For the application of an anti-monopoly law it is particularly important to define the market where a monopolist makes sales. Let us say that the Commission establishes that a milk producer is a monopolist in the Belgrade market – it can defend itself in the court by pointing out that it is only one of the many producers in the country, whose supply is small when compared with the total milk sales. Or a trading chain, which dominates the market, may claim that its sales of particular products are small in relation to the total sales (fruit, vegetable, washing powder, jams, coffee, etc.).

In Article 6 the Law regulates this problem by a tautological statement „the relevant market... is a market involving a relevant product market in a relevant geographical market". In the same Article it is stated that a relevant product market is a group of substitutable goods or services. The consumer can easily substitute one type of detergent with another, or one type of coffee with another type – indeed, we can speak about a coffee market and a detergent market. But coffee cannot be substituted for detergent, i.e. they are not substitute products. Does it mean that if a trader sells both these products, it can never be a monopolist as long as it sells the products in different markets? Or did the legislator have in mind a set of all substitute products, which then corresponds to the total market in the country, in which case again no trader can be declared a monopolist? Basically, the definition is either too narrow or too wide.

The same Article defines a relevant geographic market as „the territory within which the undertakings have been included in the demand or supply processes and where the same competition conditions apply, which are significantly different from the competition conditions in the neighboring territories". If, for example, the competition conditions are not significantly different from those in the EU countries, does it mean, according to this definition, that only the EU market is relevant? Or, if in one town or city there is a trading company which has a monopoly, in a neighboring place another company with a monopoly, in a third place a third company, etc, does it mean that the relevant geographic market is the group of all these neighboring territories? If so, then none of the existing traders will be declared a monopolist.

It is stated in the last paragraph of the same Article that the Government will prescribe the criteria for defining the relevant market. And indeed, the Government has adopted the Decree on the Criteria for Defining the Relevant Market („Official Gazette of the Republic of Serbia No. 94/05). Though we are now talking about the amendments to the Law, yet more should be said about the mentioned Decree, as it is of key importance for the application of the Law.

The Decree is totally unclear and, in many elements from the economic point of view, absolutely senseless. It was obviously drafted by an insufficiently qualified person who used foreign recommendations for defining the relevant market, i.e. it was a poor translation which revealed the lack of understanding of the subject matter. For example, in Article 1 it says that the criteria are specified for defining the relevant market, and then the next Article moves over to the „test

of a presumed monopolistic increase of prices". No connection can be seen between the two – and the question is raised how the relevant market will be defined if there is no monopoly in it. Then the Decree refers to „a presumed monopolist", as if there is a doubt that some producer is a monopolist. It is not stated anywhere that a hypothetical (speculative) experiment is in question, assumed by the analyst in order to define the scope (as to item and geography) of a market (e.g. whether carbonated and non-carbonated soft drinks make one or two markets, whether the sales in Pancevo should be added to the Belgrade market, etc.). Moreover, it speaks about the increase of the prices of a monopolist, but it does not say that all other prices and other conditions must remain unchanged, i.e. that the change of relevant prices is in question.

The Decree should be applied by the Commission which is expected to be omniscient and even clairvoyant. Among other things, the Commission should know „the nature of the production and distribution processes", „the costs that would be borne by other undertakings in the market because of their decision to offer the goods or services or substitutes", but also „the business plans and strategies of possible undertakings in the market to enter the market". To say the least, it is not clear how someone can get to know which all the undertakings in the market are, and even less how to get to know their plans and strategies, which must be secret by their nature?

All in all, the impression is that the Decree was written rather to confuse than to provide clear criteria with which the Commission can work. It is clear that, by applying this Decree, the Commission would never define the relevant market, and without it no one can be declared a monopolist, nor can mergers of competitors, which restrict the space for competition, be prevented. If there really is a serious approach to the defining of the market, the rules of the EU Commission (97C 372/03) or of the US Department of Justice and the Federal Trade Commission should be simply applied. Both these documents define the relevant market in ten pages, while the European Rules contain 58 articles, and our Decree contains only 7.

3. Dominant position

The definition of the relevant market is highly important as it is used for the evaluation of the possibilities of an undertaking to influence the level of prices and, possibly, to abuse such a position. If the

supply of the undertaking is relatively large in relation to the market size, the possibilities for the abuse of the position grow. But, if the market is defined more narrowly, the share of the undertaking is larger, and vice versa – if it is widely defined, the share of the undertaking is small. Of course, it is to be expected that the decisive influence on the level of the price is made by the undertaking which has a dominant position in the market.

In Article 16 the Law defines the dominant position as a situation in which an undertaker has the power „to behave independently of other undertakings in the market, i.e. to make business decisions without taking into account business decisions of its competitors, suppliers or buyers and/or end users of its goods and/or services". This definition makes no economic sense either. Firstly, and less significantly, it is hard to conceive a situation in which the seller's business decisions depend on the decisions of the end user of the goods he is selling, unless it is not at the same time also the buyer of his goods (it makes no difference to him whether the buyer is going to resell or present the goods to a third party). Secondly, and more importantly, no seller, anywhere, ever, including the monopolist supplying 100% of the demand in a market, can do business without taking into account the buyers, suppliers and competitors. It seems as if the definition has been taken over from a decision of a Court of Justice from 1979, which is cited in the documents of the European Commission, and which was incorrectly translated. Namely, the Court definition says that the undertaking acts independently „up to a certain level", and without these words, the sentence makes no economic sense – indeed, if the definition were applied literally, no undertaking in the market could ever be declared dominant. In the proposed amendments the words „to a significant extent" have been added in the first part of the sentence, which makes good sense, but in the second part of the sentence (after the word „or") this qualification is missing, and the changes should be made in that part as well.

It seems that this definition is abandoned in the second paragraph of the same Article when it says „an undertaking in the market may, but need not have a dominant position if its share in the relevant market exceeds 40%, taking into consideration (the Amendments add the words „its economic power") the shares its competitors have in the market, the obstacles to enter the relevant market and the power of potential competitors, as well as the possible dominant position of the buyers". The next paragraph says how an undertaking may have

a dominant position with a smaller market share than 40% as well. If someone may and may not have a dominant position, the question is what is the purpose of the 40% limit? If a limit is to be set, then a percentage should be determined and specified as dominant for all undertakings if they exceed that market share (it is one third in German legislation). In any case, if an authority declares an undertaking to be dominant in a market, then it must prove it.

The market share of an undertaking is only one of the elements which can influence its ability to dominate. It has been proved in practice that some undertakings can have a very high market share, even over 90%, and a very small market power, and vice versa – someone with a small market share can dominate the market. It seems that the legislator had this fact in mind, but it is rather awkwardly defined by Article 16.

The contemporary anti-monopoly legislations start from the position, which is missing in the Law, that, besides one's own share, the dominant position of a seller in the market depends on the elasticity of the demand for its products, and on the competitors' market shares and the elasticity of their supply. The elasticity of the supply and demand are categories without which the dominant position of undertakings in a market cannot be logically defined, and they are not mentioned in the Law at all.

4. Abuse of position

The Law does not forbid acquiring a dominant position, but the abuse of such a position. The abuse includes actions restricting, preventing or distorting competition (Article 18), and (among other things) especially, „unfair" prices or „unfair business operation conditions". However, the Law does not define „fair" prices or business operation conditions. This opens space for arbitrary interpretation of the „fairness" of these categories. Again we have a term taken from other legislations and other systems where there are strong trade associations which prescribe requirements a business operation must meet in order to be called fair, or just.

The same Article of the Law also specifies as especially gross abuse of the dominant position the application of „dissimilar conditions to identical transactions with other trading parties". In practice, it most often boils down to so-called price discrimination – when the seller

sets a different price depending on the category of the buyers. Such examples include setting lower public transport fare rates for elder citizens, lower electricity rates for households and particularly during the night hours, different tariffs in airway transport, etc. However, the price discrimination is often favorable, both for the buyers and the sellers. In many industries, producers would not be able to cover their costs without price discrimination and therefore this practice should not be declared an abuse of the market position.

5. Measures

If the Commission establishes that an undertaking has a dominant position in the market and that it abuses it, it can bring a decision by which it will specify measures the undertaking must take. The measures are imposed in order to rectify the misbalanced competition and eliminate detrimental consequences. However, the measures according to the explicit provision of Article 19 „cannot be imposed in the case of the division of a business company... the divestiture of its assets, shares or interest, the termination of an agreement or waiving of the rights enabling it to exercise a prevailing influence on another undertaking in the market". According to the Amendment to the Law this provision will be deleted and a new Article 27a added, which will allow the division of a business company, the divestiture of its shares or the termination of an agreement.

It can be freely stated that the provision, whose wording is to be deleted according to the present proposal, makes the entire Law senseless, because the purpose of the Law is combating monopoly. The very first, above mentioned anti-monopoly law from the end of the 19th century provided the possibility for the division of a business company with the aim of breaking the monopoly into a number of competing companies. This provision was applied for the first time in the case of the Standard Oil Company at the beginning of the 20th century. If the Commission cannot order the division of a monopolistic company, or order the sale of shares bought in the market for the purpose of creating a monopoly or the sale of assets bought for the purpose of restricting competition, or order the termination of monopolistic agreements, then the question is whether there is any sense in the existence of an anti-monopoly Commission. Therefore, it is no wonder that contemporary anti-monopoly laws elaborate modalities for the application of measures excluded by our Law.

The amendment of Article 70, which provided that the Commission initiates the infringement procedure against monopolies with a magistrate, is good. This Article was quite inappropriate for a number of reasons, and therefore the Amendments provide for administrative measures which will be ordered by the Commission.

6. Concentration

The Law has left an important function for the Commission, which is to give approvals for concentrations of undertakings in the market. The threshold for considering proposed concentrations has been set very low, because the total annual income of all the concentration parties should exceed 10 million euros. That means that the Commission will be overwhelmed by applications for concentration, as nowadays even small companies, in industries with a large number of suppliers, can make an income exceeding the stipulated threshold. In the Amendment text this limit is raised to 20 million euros.

When deciding whether to approve or reject an application, the Commission will first consider what effect the proposed concentrations would have on the competition, and particularly take into consideration the criteria stated in Article 28. Out of the nine criteria specified in this Article, only the last one refers to the consumers' interests, although it is one of the basic criteria in all anti-monopoly laws. Instead of that, the Law offers some quite imprecise criteria, which no one knows how to measure, such as the „structure of the relevant market" or „the domestic and international level of competitiveness of the undertakings". Although it is not explicitly stated in the Law, it can be concluded that the Commission should give approval, in accordance with Article 16 of the Law, for a concentration, if the newly formed company's sales share does not exceed 40% in the relevant market. But this can create a very high concentration of supply.

When assessing the effect of proposed mergers of competitors, the practice in Europe and the USA does not differ at all – the Herfindahl-Hirschman Index (HHI) is used. It is calculated as a result of the share square of all the undertakings in the market. The maximum value of the Index cannot exceed 10,000, which is a clear case of a monopoly supplying all the market (100x100=10000), but it can have low values close to zero in the case of a great number of undertakings. The European Commission points out in its Directives for the Application of Article 81 of the Treaty on the European Community to the agreements on horizontal cooperation (2001/C 3/02), that the market

concentration is low if the Index value does not exceed 1,000; if the Index has a value between 1,000 and 1,800, the concentration is moderate; and it is high for values exceeding 1,800. The US Department of Justice and the Federal Trade Commission accept the same intervals in their Horizontal Merger Guidelines. At the same time, these two bodies consider that if the Index after the merging of the companies is below 1,000, the probability of negative effects on the competition is small and no measures should be taken. If the post-merger Index in the zone of medium concentration is increased by more than 100 points, the anti-monopoly bodies should seriously reconsider the conditions of competition in that market, and if, in the zone of high concentration it is increased by more than 100 points, it is considered that it has resulted in the growth of the market power of the merged companies.

Suppose that there are five equally powerful selling undertakings in a market, and each with 20% of the market share. The HHI value is then 2000 ($=5x20^2$), and the European and US regulatory authorities would conclude that there is a very high concentration in that industry. Our Commission would conclude that there is no dominant company in that market as none of them has a market share close to 40%. If two companies in that market merged, again the Commission would not react as their supply covers only 40% of the market and the concentration would be approved. In the European countries and in the USA most probably such concentration would not be approved as the HHI value after the merger would be 2800 (40^2+3x20^2), which means that it has grown by entire 800 points. Therefore, it can be concluded that the application of the Law would enable the already high level of concentration in our economy to be increased much faster than in Europe and the USA.

7. Government role

The role of the Government is very highly profiled in the Law. One could say that this Law could not be applied without an active role of the Government. It is stated in nearly every article how the Government prescribes in more detail the „criteria", the „requirements", how it „regulates" a certain field, etc. Thus the Government, for example, prescribes the criteria for the assessment of the infringement of the competition, defines the notion of the relevant market, both in the geographic and commodity aspects, and prescribes the contents of the requirements for individual exemptions – requirements that must

be met by particular agreements for them to be exempted from prohibition. It regulates the contents and the procedure for the submission of applications for approval of a concentration, etc. In this way, the Government has very wide discretionary powers in matters which are technical by their very nature. It can be a significant source of corruption in a situation when the funding of political parties is absolutely non-transparent, especially when we consider the fact that the Government can, through its enactments, control the process of particular exemptions from the prohibition of competition infringement. In most countries these tasks have been transferred to an independent authority which is responsible for combating monopoly.

In the wording of the Amendment to the Law, the role of the Government has been reduced in some cases, but increased in others. Thus the Government would not prescribe the competition infringement criteria any more, but it has been given very great powers for giving exemptions to companies from the prohibition of disrupting competition. It is certainly a step in the wrong direction. The Government has assigned itself the task of drafting the Tariff of Fees, while, according to the Law, it only approves it. But the increase of the Government's influence on the personnel composition of the Commission is certainly more worrying than that. According to the Law, the Government was only one of the five authorized proponents of the Council members, while according to the Amendments, the „competent" Assembly Board alone proposes all the Council members. If we take into consideration the fact that the Government, as a rule, has the majority in the Assembly, it is clear that all the Council members will actually be elected according to the will of the Government. The provision that a Council member can be dismissed at the initiative of only twenty MPs still remains, so there is no fear that the Commission would pursue some independent policy of its own. Only the mere window dressing will remain of the independent regulatory authority, which is yet another step away from the trends in democratic countries.

8. Novelties proposed by the amendments to the law

The trend towards strengthening the Government's influence on the regulation of competition is quite clear in the Amendments to the Law. Attention should be drawn to some of them in particular. For example, the Government prescribes the requirements for small-value

agreements. They are exempted from the prohibition of competition infringement. If these amendments are adopted, companies will be in a position to freely infringe competition if their income does not exceed 10% of the sales in the relevant market. Two or more companies will be in a position to freely form a cartel if their joint income does not exceed 30% of the relevant market, under the condition that each member of the cartel does not individually make more than 5% of the income in that market. Moreover, agreements which distort competition, but which have as their object production specialization, research and development, technology transfer, and also „the distribution and servicing of motor vehicles"(?), will be allowed if the Amendments are adopted.

Directors of companies distorting competition will be relieved if the Amendments are adopted, as there will be no threat of the possibility of an injunction against their discharging their office.

The Amendments to the Law provide two more novelties: the effect of the Law should be extended to public utility companies as well, and the pardoning of persons taking part in an agreement infringing competition who have given useful evidence to the Commission about such an agreement (by analogy with a „witness associate"). The effect of these novelties will be greatly restricted – the business operation of public utility companies is already largely under state control, and the detection of secret agreements through insiders will be insignificant, as the Government will, through its new powers, first legalize the agreements of the largest companies (owned by tycoons).

9. Council's opinion and proposal

The existing Law on Protection of Competition has very serious deficiencies. Members of the professional community have already written about it. In view of this fact, it is good that the Government initiated amendments to this Law soon after it had assumed office. However, the trend of the amendments is mostly wrong. Instead of enhancing the competition process, strengthening the position and assigning new powers to the independent regulatory authority, the Government has opted to assign to itself some new discretionary powers, which will not in any case contribute to the reduction of corruption in the country.

It is not clear from the text of the Amendments, particularly from the Final and Transitional Provisions, if the Government has decided

to bring a new Law or only to amend the old one. This decision is important with regard to the destiny of the existing Commission Council for Protection of Competition, which was established only a year or so ago. In case of the adoption of a new law, a new Council would have to be elected, which would be to the liking of the present Government. Such a move would certainly mean a new blow to the efforts for the creation of independent institutions, without which, in this case there can be no free market competition with clearly defined rules, or a democratic political order as a final outcome.

Amendments to the Law on Protection of Competition would have to include at least the following elements:

1. clear statement that the aim of the Law is the protection of consumers,
2. strengthening of the role and powers of the independent regulatory authority (Commission),
3. reduction of the role of the Government, especially its discretionary powers,
4. prohibition of any disruption of competition, except in precisely defined special cases (Article 81 of the Treaty on EU and other accompanying documents, particularly the Council's Regulation No. 1/2003),
5. definition of the relevant market according to the EU Rules (EU Official Gazette 97/C 372/03) and the USA (Horizontal Merger Guidelines of the US Department of Justice and the Federal Trade Commission),
6. definition of the dominant position and the level of market strength in accordance with the criteria applied in the EU and the USA (demand and supply elasticity, the share level of the competitors),
7. assessment of the competition level in the market by the application of the Herfindahl-Hirschman Index (EU Official Gazette 2001/C 3/02),
8. elaboration of the procedures and methods of the independent regulatory authority (according to the EU Commission Regulation No. 773/2004),
9. specification of the list of bodies and institutions which must provide assistance and information to the regulatory authority,

10. provision of stable sources for funding the regulatory authority,
11. specification of the professional qualifications required for work in that authority,
12. elaboration of the punishment policy and measures imposed on legal and natural persons for disrupting competition.

The Anti-Corruption Council finds that the adoption of these amendments to the Law and their application in practice would contribute to the reduction of corruption in the country. The Council also hopes that, if this Government does not start the necessary amendments to the Law on Protection of Competition, a future Government will do it in order to bring our country closer to the rules prevailing in the civilized world.

Belgrade,
October 19, 2007

Yours faithfully,
President
Mrs. Verica Barać

ПИСМО САВЕТА ВЛАДИ ПОВОДОМ ПРИТИСАКА КОМПАНИЈЕ ДЕЛТА М И ПОЈЕДИНИХ МИНИСТАРА У ВЛАДИ НА РАД КОМИСИЈЕ ЗА ЗАШТИТУ КОНКУРЕНЦИЈЕ И САВЕТА ЗА БОРБУ ПРОТИВ КОРУПЦИЈЕ

THE GOVERNMENT OF THE REPUBLIC OF SERBIA
– Prime Minister Vojislav Koštunica –

B e l g r a d e

Dear Sir,

The Anti-Corruption Council submitted to the Government its Report on „C-Market“ on 1. October 2007. This Report was written on the basis of the documentation and relevant facts available to the Council, which is the usual practice in the work of the Council. Similar procedure was applied in the case of all previous reports which have aroused interest among the public, such as the sugar exports affair, the „Sartrid“ bankruptcy or the privatization of the National Savings Bank. Then, as now, the Council's reports were not welcomed by some people and groups whose activities were questioned, but no counter-arguments were made at the time, as is also now the case, but the work of the Council was belittled, and its members pronounced unqualified. The Council stands behind all its reports and supports all the statements made by the Council President, who does not make public statements in her own name but in the name of the Council.

The filing of criminal charges against the Council President and belittling the work of the entire Council has the aim of concealing some significant facts that have been established by state authorities, primarily by the Commission for Protection of Competition. On the

basis of the published data and the documentation in possession of the Council, we find the following facts indisputable, and the Government should take them into account:

1) The Commission for Protection of Competition brought a decision by which it did not approve the concentration between „Primer C“ and „C-market“, because these two companies would control more than 55% of the market.
2) The concentration was finalized during the course of the proceedings before the Commission, and before the final decision was brought, and the transfer of the ownership was registered with the competent authority, which was forbidden according to Article 23 of the Law on Protection of Competition.
3) Because the concentration was finalized contrary to the law, the Commission for Protection of Competition was obliged to initiate an application for the initiation of proceedings for contravention against the participants in the concentration, in accordance with Article 7 of the Law on Protection of Competition. The foreseen penalty for the company is 1 to 10% of the total annual income of the company, as well as a relief which may be pronounced against responsible physical persons preventing them from holding a managerial office (Articles 71 and 73 of the Law).
4) By the Decision of the Supreme Court of Serbia the decision of the Commission was repealed in administrative proceedings and the case remitted for new proceedings. In these proceedings the Supreme Court accepted as supplements to the claim two studies ordered by „Delta“ Co. – a study prepared by the Faculty of Law in Belgrade, signed by Prof. Vesna Besarovic, PhD, Prof. Mirko Vasiljevic, PhD, Prof. Gaso Knezevic, PhD, Prof. Boris Begovic, PhD, Prof. Dragor Hiber, PhD, and Assistant Prof. Vladimir Pavic, Ph.D. and a study by the Chamber of Commerce of Serbia and the „Conzit“ Co, signed by the President of the Chamber of Commerce Mr. Slobodan Milosavljevic, PhD, and the Director of „Conzit“ Co. Mr. Jovan Todorovic, Ph.D. The Supreme Court accepted these studies in spite of the fact that they had not been presented to the Commission, which is not in accordance with the rule that the Court brings decisions on the basis of the facts established during the proceedings. There is no doubt that these pieces of evidence could have been presented in the proceedings before

the Commission, more so because the evidence procedure was extended at the request of the party.

5) In the meantime it was disclosed that the concentration was finalized after the conclusion of a secret agreement on the fixing of the price, the division of the market and the counteracting of competitors, in the premises of „EKI Investment" Co, represented by Danko Djunic on 19 August 2005, by and between „Delta" Co, represented by Miroslav Miskovic and „C-market", represented by Slobodan Radulovic, and „Laderna", represented by Milan Beko. Such actions are forbidden by all anti-monopoly laws, as well as by Article 7 of the Law on Protection of Competition, and therefore the Commission was obliged, in accordance with Article 71 of the said Law, to file an application for the initiation of offence proceedings.
6) At this stage of the proceedings, the Commission for Protection of Competition should bring a new decision, i.e. to make a decision on the basis of the application for forming the concentration. Regardless of the fact whether the concentration has already been finalized, and that „Delta" Co. has already taken over „C-market" Co. and changed the use of many of its facilities, as well as the fact that some ministers publicly express their support of „Delta" Co, wishing to make an impression that the work of the Commission is all in vain – the legal situation must be established and the decision of the Commission is only the first step.

Regarding the stated facts, the Anti-Corruption Council requests the Government to consider the following recommendations:

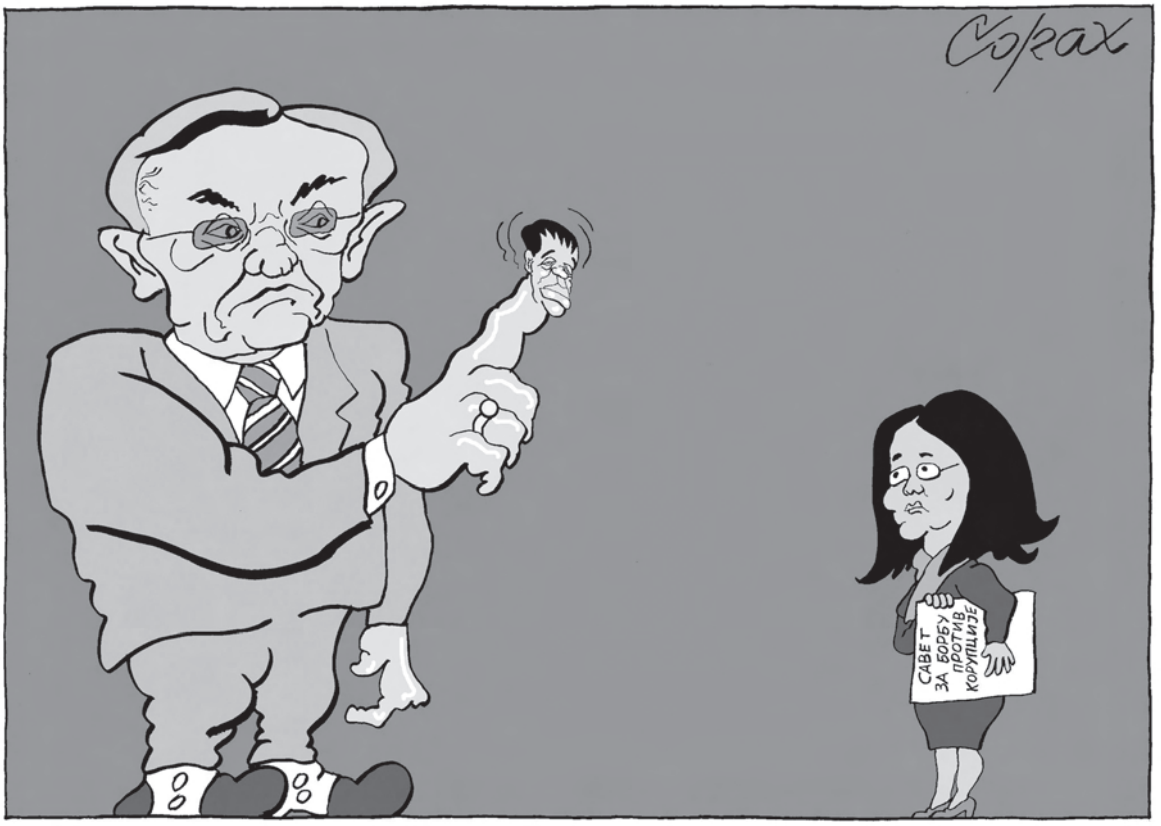
1) Starting from the UN Anti-Corruption Convention and the Initiative of the UN and the World Bank on the Return of the Stolen Property, it is necessary to examine, through the competent authorities and in cooperation with the Cypriot authorities, all the facts related to the establishment of the company „Hemslade Trading Limited" in 1991, and particularly the founding capital of that company, as well as its business operations so far;
2) It is necessary to create the best possible conditions for the work of independent institutions and regulatory authorities, in particular, for the work of the Commission for Protection of Competition;

3) In connection with this it is necessary that the ministers, in their public appearances, do not comment on the work of the independent institutions, because they may thereby impinge on their work or depreciate their reputation;
4) Ministers must not favour certain business companies in their public statements, because thereby they infringe the conditions for the exercise of free competition;
5) The Government should adopt a Code of Conduct for its members, which would, among other things, foresee that ministers make statements only within their competences and that they do not comment publicly on the work of other institutions, but to leave the evaluation of their work to the bodies authorized for that by the law;
6) We think that, until the adoption of this Code, the Government should adopt a firm position that the ministers refrain from taking part in private parties and manifestations organized by big companies, as this reinforces the impression, which already exists among the public, that big businesses fund the leading political parties.

The Anti-Corruption Council believes that the support and the trust the citizens show to the Council are significant because they indicate that combating corruption is also significant for the citizens of this country. It confirms that the struggle against corruption is possible in our conditions as well, but there is a lack of political will, primarily among the highest political bodies. The fact that the Government has ignored nearly all the reports and recommendations of this Council, in spite of the fact that they referred to highly dramatic cases of the violation of law, and of abuse and corruption, can be seen as an indicator of the lack of political will. We think that such an attitude of the Government towards the Council has contributed greatly to the creation of an environment for the campaign conducted presently against the Council by „Delta" Company. For this reason, it would be very important that the Government takes a clear position regarding the Council, and rises in defence of the public interest, and against the cases of abuse to the benefit of big businesses.

Belgrade,
November 8, 2007

Yours faithfully,
President
Mrs. Verica Barać


Сорах
САВЕТ ЗА БОРБУ ПРОТИВ КОРУПЦИЈЕ

PORT OF BELGRADE OWNERSHIP CONCENTRATION REPORT

The Anti – Corruption Council deals with individual cases only if they indicate a wider phenomenon which especially emphasizes the sources of grand corruption in politics and economy. One of these cases is the concentration of the ownership which was executed in the Joint – Stock company Port of Belgrade in the end of 2005, which remained almost unnoticed in public, but we begin to feel its effects now, and we are going to feel them in the upcoming decades as well. This case is interesting because it has all the characteristics of so called secondary privatization – a process where the shares of the employees are transferred to the richest people in the country, who have good connections with politicians and state institutions.

In a process of the secondary privatization, the foreign shell companies (companies without equity or revenues) are used in order to make an impression in public that those investments are actually foreign investments. Acquisition of shares, with a lot of speculations, is usually conducted with capital which origin is unknown, although it is usually the case that money traces lead to Cyprus and the assets which were taken out from the country during the nineties of the last century.

After successful acquisition, the new owner usually becomes the monopolist and makes remarkable profit. If the plans for construction of new business and residential objects in the area of the actual Port of Belgrade and its surroundings, which is being occupied very fast, were accomplished the new owner's profit could be measured in billions of euros. Consequently, this case is unique and arouses special attention.

Ownership concentration and monopolies

Ownership concentration, or ownership enlargement in a company, is executed when a small number of shareholders get into possession of majority interest. Consequently, it can have significant positive effects when issuing business effectiveness: the management of a company can be easier controled by a small number of owners than a huge number of shareholders, especailly when small shareholders are not completely informed about the nuances in business decision making. With strict control of the management, the owners are able to impose business decisions to a great extent, in order to enlarge the value of the company and of course, the value of their own assets. Higher company's value understands that the company's resources are used in the best possible way, which makes conditions for income growth, employment growth and the implementation of new technologies. In a word, it appears a pattern where putting the individual interests in foreground can lead to the greatest welfare for the whole society.

Such are the consequences of the ownership concentration in the rich economies where the stockholders equity (national capitalism) is widely spread. Similar effects can be noticed in those economies where markets are not so developed, but the rules are very clear and are completely obeyed. On the other hand, positive effects of the ownership concentration in our country are rare and moreover, it is common case that positive effects are overpowered by the negative ones.

Ownership concentration in our country is carried out in specific conditions, without totally completed rules, or the current legislation is not fully applied in practice.

It seems that two particular elements are especially emphasized here, and that is the crucial influence of political factor on economic issues and a fact that the capital which was taken out from the country during nineties plays a dominant role on capital market. These factors contribute to the creation of such ambient which is suitable for the grand corruption flourishing and even more, they create an inefficient economic system where so called big players, who have created a special political – economic monopoly have a prevailing role. Namely, the big capital is interested in acquiring major interest in companies which already posses, or which can easily accomplish, the dominant position on the market. The easiest way for accomplishing that aim is, at first, providing ownership concentration in the corporation through political influence and thus providing a dominant position on the market.

Every monopoly is economically inefficient, because it often offers goods with higher prices than concurrent bidders, it produces less, its expenses are higher and resources insufficiently employed. When a monopoly's position is protected by political support the negative consequences are long-lasting. It is possible that this rule would be confirmed unless the Government made resolute turn regarding its position towards market concentration and manipulations in a process of ownership enlarging in the companies with strategic importance.

Ownership concentration which has been carried out in the Port of Belgrade is an example of monopoly creation under protection of political factor and with an active participation of "runaway" capital.

Legislation

Law on Market of Securities (Official Gazette of SRJ no. 65/02 and Official Gazette of Republic of Serbia no. 57/03) regulated the takeover process of corporations during the time when the ownership concentration in Port of Belgrade was carried out. According to this law, share trading could be carried out only on the regulated market – stock market (Article 52) – and if a purchaser exceeded the limit of 25 % it would be obliged to request for a purchase approval from the Republic Of Serbia Securities Commission (Article 69). This way of share acquiring is called the takeover proposal and it was specially regulated (later on, the Law, which laid down the takeover issue, has been passed).The purpose of provisions is to disable possible abuses either on the side of supply or on the side of demand. According to the Law on Market of Securities the Commission has been empowered to regulate the entire process. In connection with this, the Commission specifies the contents of a bid which must be filled out in a special form by a purchaser and sent to all shareholders.

The contents and form of the takeover bid proposal are specified in the Code of rules (Official Gazette RS no. 102/2003, 25/2004, 103/2004, 123/2004), which was adopted by the Republic Of Serbia Securities Commission. The Code has been amended several times, but at the time when the takeover bid for the Port of Belgrade was submitted, Article 7 specified all necessary documentation which should be attached with a request by a potential purchaser. The integral part of the Code are the Guidelines which bring more detailed definition of what the takeover bid should consist of. Item 4 of the Guidelines emphasizes that the data of the targeted Joint Stock Company (whose

shares are about to be purchased) have to be given e. g. the value of property and capital, as well as other relevant data regarding the Joint Stock Company should be well known to a bidder. Item 5 defines data regarding bidder, inter alia the value of its core capital (for a company, not for an individual), data about individuals who have more then 1/10 votes in the Assembly of a bidder, data regarding statement of assets and liabilities and profit and loss account etc. If all data were available and if those data were in accordance with other notified documentation the Commission would approve the takeover bid (Article 8 of the Code).

Board of Directors of a Joint Stock Company has the most reliable information regarding the affairs of a company business. The Law, in Article 72, foresees that the Board of Directors can, within a period of 10 days from the day of the takeover bid submission, notify shareholders about a bid and instruct them on decision making (whether to accept the bid or not). In its notification the Board is obliged to disclose all information about important changes which have occurred from the day of conducting the last financial report, in other words, annual report (Item 8 of the Guidelines about contents and form of the Board notification referring to the share takeover bid).

Concentration in practice

Port of Belgrade covers the area of about 220 hectares of land in the central city area between Francuska street and Pančevo Bridge (municipalities Stari grad and Palilula). Master plan of Belgrade until 2021. (Official Gazette of city of Belgrade no. 27/03), in Item 4.4.9 foresees that Port of Belgrade should remain the business area, which is also planned to be widened. Only three years after the Belgrade Master plan has been issued, which defines the purpose of the land until 2021, the Belgrade Land Development Public Agency, on 27. December 2006, notified Public invitation for conducting the preliminary advisability study with a master project for a new mechanized cargo port in Belgrade. Public invitation came after the share takeover of the Port of Belgrade in September 2005. Apparently, the change of the purpose of the land and the port relocation had been previously agreed, and the Belgrade Land Development Public Agency was supposed to conduct and justify that agreement by ordering the advisability study.

Although the Master plan has not been changed and no decision on purpose of the land modification and relocation of the port

has been issued, the acting Mayor of Belgrade Mr. Zoran Alimpić presented the new port project in November 2007. On that occasion he told that "Master plan until 2021 and Master plan of inland waterways of Serbia until 2025 foresee the construction of a new cargo port on the Danube. The location on the right bank of the Danube, from Dorćol to Ada Huja of 480 hectares, where the port is currently located, is to become the area for construction of business-residential buildings". (Glas Javnosti 6. 11. 2007).

The actual port is located on the potentially most attractive spot in the core down town, because the building of the business-residential complex is also planned on the nearby, downstream land on the area of 500 hectares. Regarding this matter, it is obvious that both the land of the port and the downstream land have the great value.

Port of Belgrade company, which uses above mentioned 220 hectares, was privatized in 1998 according to the at the time existed Law on Ownership Transformation, when the 60% of the shareholders capital was divided to the employees for free, 30% was transferred to the Share Fund and 10% to the Pension Insurance Fund. The assessment of capital value was carried out with the current account from 31.12.1998. As the assessment was significantly bellow the market value, the management of the company decided to conduct a new assessment of the capital value in 2005. Regarding this issue, the Institute of Economic Sciences was commissioned in the April of the same year.

The Institute submitted the preliminary results to the company in June 2005, when stated that there were some important differences (over 3.5 times higher) between the accounting value and capital value which was obtained by implementing the international accounting standards. In the same month the management of the company informed the Ministry of Justice, Share Fund, Privatization Agency and the Securities Commission that there was a modification regarding assets value which caused the change regarding capital value and that it was in the best interest of shareholders including the state, as the individually biggest holder, to wait with the selling of the shares.

However, although the Institute did not finish its work, i.e. the capital value in the balances of the company has not been modified, the Board whose members were professor Dr Vladeta Čolić, the president, Vladeta Blagojević, professor Dr Mirko Vasiljević, Miroslava Drobac, Dušan Kosovac, as members, scheduled the Annual Shareholders Meeting for the 9. of September 2005. On that meeting, financial reports were discussed and the business policy was adopted. On that occasion,

the management informed shareholders about the contract which had been signed with the Institute, but the financial reports were adopted without previous adjustment of the capital value. Supervisory Board (professor Dr Danijel Cvetićanin, the president) also omitted to warn the Assembly on that fact, so the shareholders stayed in delusion that the value per share was 494 din.

The day the meeting was held on September 9, 2005. The Securities Commission approved the bid of the Worldfin company from Luxemburg for takeover of the Port of Belgrade. The bid was issued through the BDD M&V Investments from Novi Sad (the same firm had participated in purchase of C Market shares). The text of the bid was published in the next day daily newspapers. The offer was opened until September 30, and according to it the share price amounted 800 din. The Board of Directors informed the shareholders by an advertisement on September 21. It cited that the assessment of the capital (property) value of the Port of Belgrade was in process and since the actual value was higher then the accounting one, the Board recommended the shareholders to wait until September 23 "and that they should, after the deadline has expired, depending on whether there are some other competing bids or not, decide to deposit shares, in order to sell them, or not."

Until September 23, not one competitive bid had occurred and the shareholders disposed their shares. The Institute submitted its findings on September 27, and based on them the share price was 1774 din. The very same day The Privatization Agency decided that the takeover bid was accepted and it issued an instruction to the Share Fund to sell all the shares in possession (40,88% shares). The takeover bid was successful and Worldfin acquired more then 93% of Port of Belgrade shares. Share price which was paid amounted 800 din.

Worldfin company from Luxemburg, which purchased the shares, was registered in Rue d'Arlon 207, just as the Novafin company which acquired C Market shares only a few days after it was founded. In its takeover bid the Worldfin stated that it is a new company, so there were not any balances or financial reports. According to the Court Registrar registration certificate, core capital value of this company was 31.000 EUR. The company does not have a share in the core capital of other legal entities.

Unanswered Questions

The first thing is, how is it possible that a company which core capital amounts 31.000EUR and which does not have any connection with other legal entities can pay almost 40 million EUR for Port of Belgrade shares. Almost in the same period (the end of 2005) the same pattern was used when the small C – market shareholders` shares were purchased – the shares were purchased by a company without any turnover or property, except the minimum start-up capital and the amount was 44 million EUR. It is more then clear in both cases that the shares were purchased for another purchaser who stayed in the shade. How did the Securities Commission overlook these facts and why The Administration for the Prevention of Money Laundering did not react?

Why did the Commission approve the takeover bid in spite of some contradictory statements? Namely, the bidder emphasizes that "it does not have any information about assessment of capital or assets" and that "there are not" any other important data regarding Joint – Stock Company that are well known to the offeror. On the other hand, the offeror states that there were some contacts with the management of the company. It is not realistic to think that the people from the management while contacting potential purchaser avoided to mention that the accounting value was to low and that the revaluation proceeding was in process. In other words, if they did avoid that, they were acting in the purchaser's favor and not in favor of its own shareholders and according to it, the Commission was obliged to react. The Commission was also informed on capital revaluation, so it could inform the offeror on that matter. So, it is clear that the purchaser had a key information and it did not want to include it into the takeover bid.

Another information which can be noticed is that the Worlfin company was registered on the same address as the Novafin company which acquired the retail store chain C – market. According to the testimony of Mr. Milan Beko before the Special Department of the Belgrade District Court in the proceedings against Mr. Slobodan Radulović it is obvious that it is not just a pure coincidence. The witness stated that the Novafin company "was established for that purpose" and that it is a common thing in that kind of business to establish "companies for special purpose without direct connection with their names – they are taken out from the drawer". On that occasion the witness also stated that he runs number of companies, he called them "shell companies",

which do not have any turnover. They have been founded for accomplishing of a concrete task. Novafin`s task was purchasing of C – market's shares and Worlfin`s task obviously was purchasing of the shares of Port of Belgrade. How is it possible that none of the state institutions have reacted on the public confession regarding the role of the shell companies?

In both cases the price which was paid to the shareholders was significantly lower then the actual one, but moreover, the fact that concerns the most is that it was done in favor of the owners who had remained undeclared. Regarding C – market issue The Commission for Protection of Competition has ascertained that the Hemslade Trading company from Cyprus, which is the owner of Delta Holding, has purchased the shares of C – market which led to the monopoly position of that company in grocery retailing. In the Port of Belgrade case the actual owner has not been officially established yet, but however, regarding the above mentioned, the assumption that it is the same owner is pretty convincing. In the first case the majority shareholder had a monopoly position in retail trading, and in the second case the major part of the free urban building land in the central area of Belgrade. The question remains, why no one of the state institutions or officials (either on state or local level) has mentioned the establishing of the monopoly which exceeds the frames of a particular economic branch?

How can we explain the synchronized acting of state institutions, shares` purchaser and the management of the company during the purchasing process (ownership concentration) in the Port of Belgrade? It can be easily noticed from the dates and contents of the particular events:

- The Board was officially informed, latest in June, that the actual property value of the company was much higher then accounting one. Because of that, state institutions were informed on this matter. However, the Board scheduled a shareholders meeting before receiving the final value assessment and state institutions did not react.
- On the day of the shareholders meeting the Securities Commission approved the takeover bid ignoring the major difference between the accounting and the actual capital value.
- In the takeover bid, it is stated that the representatives of purchaser have had a conversation with the management of the company about the possibilities of purchasing shares of the company and they sent an investment letter of intent. The As-

sembly of shareholders was not informed about these issues. The Board did inform shareholders by an advertisement that the offered purchasing price was too low, but it also recommended that shareholders should decide on the issue depending on whether there were some other competitive offers until September 23 (the closing of the offer was on September 30, although the Worldfin accepted an obligation for purchasing the shares, under the offered price, for 20 more days from that date).

– Privatization Agency issued an order to the Share Fund to sell the shares of the Port of Belgrade the very same day when the final value assessment was issued, although it received information that the bookkeeping capital value of the company was unreal, three months earlier. That way the State has lost at least 21million EUR which is an amount of the difference between the estimated value of the purchased shares and the price which was paid.
– The State decision to accept the offer three days before the closing sent a direct message to the small shareholders that they should also accept the offered price. Maybe it is not worthless to mention a fact that the official representative of the Worldfin in the takeover process of the Port of Belgrade was Mr. Vuk Delibašić (the director of Primer C, appointed by Novafin company, the company which temporarily took over the shares of C – market) the person that was employed in the Privatization Agency until the end of 2002. Also, the Executive Director of the Agency Mr. Goran Mrđa who was in position until the end of 2005. is currently member of the Board of the Port of Belgrade.

Finally, one can ask a question why are the Belgrade citizens forced to build a new port on the Danube in order to give away the most attractive urban building land to the company without equity or revenues?

Recommendations to the Government

The liability of the participants in this process should be examined by the authorized state institutions. It is Government's responsibility to recognize all system's consequences of this and similar cases.

At the very beginning of this report it was pointed out that the ownership concentration in market economy is often very prosperous because it increases the owner's (principal) extent of control over the management of the company (agent). There is no doubt that the similar effects could be expected in our economy if we could eliminate the negative conditions regarding concentration process. However, one must pear in mind – macroeconomic consequence of the ownership concentration, which cannot be fully expressed in the developed economy.

Ownership concentration significantly reduces the number of shareholders in our country. It also reduces the credibility of the capital market and readiness of people to invest in shares. For example, with the concentration in companies C – market and Port of Belgrade the number of shareholders of these companies decreased from 9624 to 1058, where every one of the small shareholders (individually or collectively) is disabled to influence the company's business policy – in both cases, only one owner makes all key decisions.

In situation like this in our country, where the corporative managing is underdeveloped i.e. where small shareholders` interests are not respected, the most important thing in practice is to provide over 50% majority at the Shareholder Assembly in order to accomplish a full control over the company and to impose the major owner's will.

The consequences are multiple: potential investors are not interested to invest into companies where they can not have major ownership, the price of minority shares remains permanently low and the capital market cannot escape from the vicious circle of underdevelopment. Simply, people are not confidential regarding investing in minority shares and on the other hand, the major owner is not interested in purchasing minority shares because it controls the company without those shares. Accordingly, the stock market transactions of such companies are insignificant and they just formally exist on the stock market listing.

Without fully developed capital market, the offer and demand of available financial property must be carried out only through the banking sector. As the competition in this sector here is still not the rule, and agreement is an exception, but vice versa – the competition is an exception – the interest rate must be high, so it is rare to find some profitable projects. All these facts lead to decrease of economic development and to the high unemployment rate on long-term basis as well.

The Government has to be aware of all these macroeconomic consequences of its acting, in other words non acting. Regarding this particular case, it has to take into consideration the fact that the ownership concentrations, like in Port of Belgrade, C – market, Knjaz Miloš, and in many other companies as well, create prerequisites for permanent nonfunctioning of the capital market.

On the other hand, the way of dealing these concentrations, accompanied with a number of frauds, with acting of state institutions in favor of the big capital, with bending the law by overlooking indisputable facts or regulations, contributes to the growth of the instability of property rights. In our country, small shareholders cannot be sure that their legal rights will be obeyed – the dividends are not paid, even if the company makes profit, and the profit is often unexpressed through "creative bookkeeping". The only option for the shareholders to sell their shares is the stock market, but even there, they are faced with the underestimated value of their shares. Accordingly, it is not weird that the small shareholders strive to get rid of their propriety rights. The acting of the state institutions, first of all the Privatization Agency and the Share Fund, only strengthens the insecurity of property rights, which can easily be seen in this particular case. Without the security of property rights there is no development of market economy and finally of the democratic political system as well.

The Government has to be aware of all political consequences of the ownership concentrations like it was done in the Port of Belgrade and C – market. Both ownership concentrations were carried out through firms that were registered abroad in order to participate in the privatization process. The capital they use is of unknown origin, although in one particular case it was realized that it came from Cyprus. That capital is managed by the people who were highly ranked in the Milošević's regime (Miroslav Mišković and Milan Beko). This fact should not be underestimated and the Government's task is to investigate(together with Cyprus authorities) what was the amount of the capital outflow during nineties, which are the channels of the capital current and to identify the cases where it was legalized in the privatization process. This should be carried out in cooperation with specialized international institutions referring to the provisions of the UN Convention against Corruption (Articles 46 and 48). This is not just a necessity, but also an obligation for the Government since our country, besides the UN Convention, has ratified the Council of Europe conventions against corruption.

The participants of above mentioned concentrations are among the richest people in this country and they strive to enlarge their wealth by creating monopolies. By purchasing the C – market shares they have created the retail sector monopoly and the first step in monopoly of residential building at the most attractive locations in Belgrade was done by purchasing the shares of the Port of Belgrade.

This report shows, like the report on C – market, that it is impossible to create a monopoly without support of the state. Thus, the potential monopolists are naturally interested in securing the state support for their activities and that is one of permanent resources of grand corruption. On the other hand, creating a monopoly causes the permanent source of the economic inefficiency – monopoly charges customers higher price, pays lower price to the suppliers and anyway, it engages less capital and labor than in the case where the competition existed. Accordingly, the direct task of the Government is to improve the competition on the market and to support the acting of Regulatory Bodies, first of all the Commission for Protection of Competition.

One of the basic constants of all democratic governments from 2000. was support to the privatization process without the questioning the sources of capital. Such approach led to the legalization of illegally acquired wealth, but also to the great split within society. Serbia has become a country of poor citizens and extremely wealthy individuals. This situation contributes to the growth of grand corruption, first of all by the non transparent financing of the political parties. However, the consequence of that fact, which is maybe more important, is that the extreme polarization regarding wealth cannot be suitable for strengthening of the democratic political system. The extreme gaps in wealth lead to the extreme political positions and they do not contribute to the strengthening of democratic values in a society.

Belgrade,
February 19, 2008

Yours faithfully,
President
Mrs. Verica Barać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ANALYSIS OF THE REGULATION ON CRITERIA AND PROCEDURE FOR CALCULATION OF COMPENSATION FOR CONVERSION OF RIGHTS FOR PERSONS ENTITLED TO CONVERSION AGAINST COMPENSATION

GOVERNMENT OF THE REPUBLIC OF SERBIA
– Prime Minister, Mirko Cvetković –

B e l g r a d e

Dear Sir,

The Government of the Republic of Serbia has adopted the Regulation on Criteria and Procedure for Calculation of Compensation for Conversion of Rights for Persons Entitled to Conversion against Compensation. The authorization for the adoption of this Regulation is contained in Article 108 of the Law on Planning and Construction (*Official Herald of the Republic of Serbia* No. 72/09 and 81/09), which provides for that the Government may prescribe in more detail the criteria and procedure for calculation of compensation for conversion of the right to use building land into the ownership right against compensation.

The Anti-Corruption Council finds that this Regulation is unconstitutional, contrary to the Law and economically harmful, for the following reasons:

1. Our Constitution does not allow adoption of Regulations which have the effect of a law. Regulations are by-laws which elaborate provisions of laws in more detail and they cannot have provisions which regulate material law, and Regulations cannot be in contradiction with provisions of a law.

Article 3 of the said Regulation regulates that the conversion compensation is calculated so that the market value of building land at

the moment of conversion of the right of use into the ownership right is reduced by the costs of the acquisition of the right to use the building land, as foreseen by Article 103, Paragraph 1, of the Law. However, Article 4 of the Regulation does not specify in more detail the provisions for calculation of the costs of acquisition of the right of use, but the revalued price of capital is recognized as the cost of acquisition.

When the Law prescribes that the conversion compensation is calculated so that the cost of acquisition of the building land is deducted from the market value, then these costs cannot be equated with the price of the property or capital. The obligation of the Government was to specify in more detail which costs of the acquisition of land are recognized and in what way their amount is calculated. The Law did not foresee that the costs of acquisition of land are equal to the price of the capital and property, and consequently it cannot be provided for by a Government Regulation either. Acting in this way the Government has, actually, changed the material-legal meaning of the provision of the Law.

2. The Regulation, Article 8, Paragraph 5, provides for the possibility of the conversion of the right to use undeveloped building land into the ownership right for business entities and other legal entities to which the provisions of the Law regulating privatization, ownership transformation, bankruptcy and execution procedures were applied. The Law on Planning and Construction does not foresee the possibility of conversion of undeveloped land for these entities, and therefore, this right could not be provided for by the Regulation either. The Law did not provide for the conversion right on undeveloped land because in the privatization procedure and in the other referred procedures it was not possible to obtain the right to use undeveloped building land which was state-owned and was not on sale. It is building land which cannot be disposed of from the state property according to the Law on Planning and Construction (*Official Herald of the Republic of Serbia* No. 47/03 and 34/06).

The right to use developed city building land was acquired by transfer of the ownership right on the legally built buildings on that land, and the land followed the legal destiny of the building. The right to use undeveloped building land could not be acquired in the privatization procedure because there were no buildings on which the ownership right could be acquired and the subsidiary right to use that land.

3. The recognition of the price of capital paid by a legal entity in a privatization procedure for a company in whole, as costs of acquisition of the right to use the building land, is economically unacceptable and it virtually means giving a gift of great value to owners of privatized companies which paid nothing for the state-owned building land because in the procedure of privatization and assessment of the value of capital value of the building land was assessed as zero. The price of capital is the compensation for the Company excluding the state-owned building land though it is included in the costs of acquisition of the right to use the building land, which is economically senseless, so that we have a situation that state-owned building land is entirely given as a gift to the buyers of privatized companies, or if the building land is partly paid, then the privatized company is entirely given as a gift. A good example is the case of *Luka Beograd*: the owners are in position to convert the right of use into the ownership right over 120 hectares of the city building land against the payment of certain compensation for these 120 hectares of the land, but in that case they get all the property of *Luka Beograd* free of charge, as the present market value of this land is higher than the total price of the capital that was paid for *Luka Beograd*. Or if we take a hypothetical example: if a company X was paid EUR 10 million in a privatization procedure, and the owner has acquired the right to use some land whose market value is now EUR 2 million, he will get the land free of charge, as all the EUR 10 million he had paid for the company in general are recognized as the cost of acquisition of the right of use. Obviously it is an absolute absurdity, which, unfortunately, has a high price and means an unacceptable redistribution of resources, and mostly in favour of those who entered privatization transactions deliberately, not to restructure and make the purchased companies more effective economically, but to come into possession of valuable building land, without having to pay anything for it and thus unlawfully acquire great benefit, and of course, at the expense of the State and the citizens.
4. The Regulation, Article 7, provides the possibility that the right to use undeveloped state-owned building land acquired for the purpose of development, be converted into the ownership right. The application of this provision creates the possibility to convert the right of use into the ownership right also on land where the time to put it to the intended use has expired, but the right to use the land has not been denied, either because government authorities have not updated the data, or because of corruption. The Regulation provides

the possibility that unlawful transactions may be legalized – and in many cases it will be possible to acquire the ownership right of undeveloped land for which the grounds for the right of use ceased to exist long before.

The Anti-Corruption Council suggests that the Government recalls the Regulation on Criteria and Procedure for Calculation of Compensation for Conversion of Rights for Persons Entitled to Conversion against Compensation within the shortest possible time because the application of this Regulation would mean jeopardizing the public interest and acting contrary to the Law on Planning and Construction. The Regulation would enable redistribution of huge State wealth to the accounts of privileged individuals.

The Anti-Corruption Council suggests the Government to adopt a new Regulation in accordance with the Constitution and the Law which will provide that the compensation for the conversion of the right of use into the ownership right over building land be calculated so that the market value of the building land is reduced by the real costs of the acquisition of the right of use. The real costs of acquisition of the right of use may be considered also to be the value of the right to use the building land if it has been recorded in the books, or in the Report of the Assessment of the Value of the Company on the basis of which it was privatized. The market value should be also reduced by possible costs sustained by the applicant for the conversion in the period from acquiring the right of use until the submission of the application for conversion, and which were related to development of that land, building of its infrastructure, as well as possible expenditures resulting from the increase of the value of the land. Of course, all these costs can be recognized up to the level of standard costs for these purposes.

Yours faithfully,
President
Mrs. Verica Barać

Cc: Government of the Republic of Serbia, Prime Minister, Mr. Mirko Cvetkovic, PhD
Minister of Environment and Spatial Planning, Mr. Oliver Dulic
Minister of Finance, Ms Dijana Dragutinovic, PhD

INITIATIVE TO ASSESS THE CONSTITUTIONALITY AND LEGALITY OF ARTICLE 4, PARAGRAPH 1, OF THE REGULATION ON CRITERIA AND THE PROCEDURE FOR THE CALCULATION OF THE LEVEL OF COMPENSATION FOR CONVERSION OF RIGHTS FOR PERSONS WHO ARE ENTITLED TO THE CONVERSION AGAINST COMPENSATION

TO THE CONSTITUTIONAL COURT OF
THE REPUBLIC OF SERBIA

B e l g r a de

According to Article 103, Paragraph 1, of the Law on Planning and Construction, the right of use of the state-owned or public building land, held by business entities and other legal persons, as well as their legal successors, to whom the provisions of the Law regulating Privatization, Bankruptcy and Execution Procedures are applied, may be converted into the ownership right against the compensation of the market value of that building land at the time of the conversion of the right reduced by the amount of the costs of the acquisition of the right to use that building land.

The said provision of the Law is quite clear, i.e. it is quite clear that the conversion of the right of use into the ownership right is effected with the payment of the compensation of the market value of that land, where the market value is reduced by the costs of the acquisition of the right to use that building land.

According to Article 108 of the Law, the Government is authorized to define criteria and a procedure for the calculation of the level of compensation for persons who are entitled to conversion by the Law.

On the basis of this Article, the Government adopted the Regulation on Criteria and the Procedure for the Calculation of the Level of Compensation for Conversion of Rights for Persons Who Are Entitled to the Conversion against* Compensation.

In Article 1 of the said Regulation, the Government defined the criteria on the basis of which the market value will be established for the building land that is the subject of conversion and it was done in accordance with the powers provided for in the Law, and in accordance with the text of the above mentioned Articles of the Law on Planning and Construction.

However, by Article 4, Paragraph 1, of the Regulation, the Government regulated that the costs of the acquisition of the right to use the building land include the total revaluation price of the capital or property, paid in the privatization procedure, or in the bankruptcy and execution procedures.

In this way, and by regulating the costs in this manner, the Government went beyond the framework provided by the Law since the framework provided by the Law stipulates that the market value is reduced only by the costs of the acquisition of "that land" and not by the price of the total capital, which is a huge difference.

In order to establish what it means and what consequences the State will have, we have to determine in clear terms what the price of the capital and the price paid for the acquisition of the right to use the particular land are.

In accordance with the International Accounting Standards, applied under the Law on Accounting, the capital of a business entity is the amount calculated by establishing the value of the total property of the entity (which includes all immovable property, facilities, equipment, stocks and shares in other business entities and other rights, i.e. everything that the entity owns) and upon subtracting from that amount all the liabilities of the entity incurred on any basis. The balance arrived at in this way is the capital. In order to determine the capital in exact terms, the procedure is preceded by the assessment of the property of the business entity. The right of use was not assessed during privatization since this right is not the ownership right and includes no right of disposal, and the State, as the owner, could appropriate the said right of use from one person and grant it to another person to exercise it in the light of Article 8 of the Law on the Assets Owned by the Republic of Serbia.

Consequently, the price paid for the acquisition of the capital of a business entity in the privatization, bankruptcy or execution procedures is not the price paid for the acquisition of the right to use the building land that is the subject of conversion, and therefore the price of the capital cannot be the amount by which the market value of the land is reduced.

The consequences of the adoption of the Regulation by which the Government goes beyond the framework of Article 103, Paragraph 1, of the Law on Planning and Construction providing for a fair compensation based on the market value of the subject of conversion and on the reduction of the amount that the buyer paid for that land produce very serious consequences, such as:

1. Instead of establishing the price of the acquisition of the building land, which can be established very simply on the basis of the assessment of the property of a business entity, which always precedes the said privatization, bankruptcy and execution procedures and only by the revaluation of that price where the amount arrived at in that way is reduced by the established market price, according to the Regulation the market price is reduced by the price of the capital which includes not only the potentially assessed right to use the land, but also all the buildings, equipment, shares and stakes held in other companies and all receivables, which is another economic and legal category, different from the price of acquisition of only a particular land that is the subject of conversion. If, at the time of the sale of the business entity or its property, a lower price has been achieved that is then* the assessed value of the property, then the price of the converted immovable property is calculated by establishing what is the percentage share of the value of the land in the assessed value of the property, and the percentage of the achieved sales price established in that way is used for the reduction of the market value of the land in the conversion procedure.
2. If no assessment has been made, a solution is available in this case as well, because the price of the acquisition of a building land is established from the adjusted book price of the building land being the subject of conversion.
3. If the subject land has not been evaluated in any way in the above-referred procedures, it is clear then that the buyer had no costs of acquisition of that building land, or that he did not pay for it in the said procedures in any way and that there is nothing to deduct from the market price (no amount can be recognized if he has not paid any).

4. If the price paid for the capital (which includes all the property of a company) were recognized as costs of the acquisition of a particular building land, then the buyer would receive as a gift either the building land or the equipment and other property since it often happens that, once the established market price of a building land is reduced by the amount of the price paid for the capital, no amount shall remain that covers the acquired equipment or other property.

The problem is resulting from the fact that the State did not regulate the public property by law first and only then started the privatization.

Any serious investor was aware that the right of use does not constitute ownership and, as a consequence, such investors often refrained from buying. However, our "tycoon investors" have not been interested at all in the absence of the legal regulation of the property (the right of use); on the contrary, it suited them, because by buying they achieved a number of goals: they laundered money, were given companies by and large at very low prices (just because of unregulated property that was not a subject of assessment either) and, in doing so, they knew that, with the helping hand of the Government as it is, they would convert the right of use into ownership; actually they knew in advance that they would be able to exert influence to get things done exactly the way they are done now by this Regulation, all under the guise of the protection of investors.

Material Law

According to Article 3 of the Constitution, the rule of law is the basic principle of the Constitution and is rested on inalienable human rights. The rule of law provides, *inter alia,* for the compliance of all government bodies with the Constitution and laws.

According to Article 84 of the Constitution, everyone has equal legal status on the market and acts, which, contrary to law, restrict free competition by creating or abusing monopolistic or dominant status are prohibited. Rights gained through capital investment in accordance with law cannot be curtailed.

According to Article 86, Paragraph 3, of the Constitution, public property resources may be disposed of in the manner and under the terms stipulated by law.

According to Article 167, Paragraph 1, Point 3, all general acts must comply with the Constitution and law.

According to Article 194 of the Constitution, the legal system of the Republic of Serbia is uniform, the Constitution is the supreme legal act and all laws and other general acts adopted in the Republic of Serbia must be in compliance with the Constitution.

According to Article 195 of the Constitution, all by-laws in the Republic of Serbia must be in compliance with law.

We find that the Regulation is not in compliance with the Law and Constitution.

Privatization, bankruptcy and execution have been effectuated with an altogether unregulated public property and the right of use as an ownership element. The unregulated status prevented many serious investors to make investments because they knew that no ownership was included in the purchase and that it was not clear when and in which way the State would regulate the public property matter. Purchases were made only by privileged investors who knew that they would be able to exert influence on the Government to grant them the ownership of the land free of charge.

Accordingly, these actions prevented competition, because only the privileged investors with the knowledge of confidential information were in position to invest, because they knew that the Government would adopt this Regulation by which the city building land would be given them as a gift. This operation violated the basic human right, the rule of law and the constitutional principle from Article 84 providing for equal legal status on the market for everyone, without any privileges. The rights acquired through capital investment cannot be curtailed or increased, which means that only what the buyers have invested in the purchase of land and nothing else can be recognized to them in the privatization, bankruptcy or execution. According to Article 86 of the Constitution, public property resources may be disposed of in the manner and under the terms stipulated by law; if the Law on Planning and Construction stipulates that, in the conversion procedure, only what the buyers have paid for the acquisition of the land being the subject of conversion will be recognized to them, then* that stipulation then cannot be declined from in the Regulation as a by-law and recognize the amount paid for the capital as it is in contravention of the said constitutional and legal provisions.

An analysis of the contents of the provisions of Article 4, Paragraph 1, of the Regulation on Criteria and the Procedure for the Calculation of the Level of Compensation for the Conversion of Rights for Persons Entitled to Conversion against* Compensation and the provisions of Article 108 of the Law on Planning and Construction show that the said provision of the Regulation is in contravention of the provision of the Law, which makes it unconstitutional and unlawful.

As a matter of fact, by adopting the contested provision of the Regulation, the Government has exceeded its constitutional powers provided for in Article 123 of the Constitution which reads: "The Government shall adopt: [...] regulations and other general acts for the purpose of law enforcement." In the concrete case, the Government regulated by the Regulation as a general by-law the matter that is regulated by law, and established a solution which is contrary to the stipulation contained in Article 108 of the Law on Planning and Construction. Thereby it has violated the constitutional principle (Article 195) according to which all by-laws of the Republic of Serbia must be in compliance with law. Thus the contested provision of the Regulation violates the explicit provision of Article 86, Paragraph 3, of the Constitution, as well as the constitutional principle regarding the division of power into legislative, executive and judiciary.

Considering the above stated reasons, we suggest that the Constitutional Court of the Republic of Serbia brings a decision by which it will rule that the provisions of Article 4, Paragraph 1, of the Regulation on Criteria and the Procedure for the Calculation of the Level of Compensation for the Conversion of Rights for Persons Entitled to the Conversion against* Compensation are not in accordance with the Constitution and law.

Yours faithfully,
President
Mrs. Verica Barać

REPORT ON PRIVATIZATION OF THE COMPANY *NOVOSTI*

1. Privatization According to the Previous Regulations

The privatization of the socially-owned company NIP *Novosti a.d*. Belgrade started in 1991 by the payment of internal shares according to the Law on Socially-Owned Capital (Official Gazette of the SFRY No. 84/89 and 46/90). The privatization was continued in 1998 according to the Law on Ownership Transformation (Official Gazette of the Republic of Serbia No. 32/97). On 14 July 1998 the Directorate for Evaluation of Capital issued the Decision No. 647/98–1–6 by which the evaluation and the capital ownership structure were verified after the completion of the first round of the ownership transformation. The federal public institution *Borba* initiated an administrative dispute claiming the revocation of this Decision because *Novosti* had changed its status by separating from *Borba* without its approval as the parent company and without making separation Balance Sheets. Deciding on the *Borba* complaint, the Higher Commercial Court delivered the judgment Urs. No. 84/99 on 16 February 2000, by which the complaint was accepted, and which superseded all previous decisions on the ownership transformation of *Novosti*.

After this judgment had been passed, the Directorate for the Evaluation of Capital issued the Decision No. 647–1/98–23 on 29 February 2000, by which it revoked all of its previous decisions related to the transformation of ownership, as well as all relevant decisions and the public call for the registration of the shares in the first and second rounds of the ownership transformation issued by the Shareholders' Meeting of the company *Novosti*. After the revocation of the ownership transformation, *Novosti* was affiliated with the Federal State-Owned Institution (SJU) *Borba* by the Regulation on Amending the Regulation on the SJU *Borba* (Official Gazette of the FRY, No. 10/2000).

As all the decisions and the ensuing actions based on them were revoked by the court decision, the decision of the Directorate for Evaluation of Capital *Novosti* was not in the process of ownership transformation at the moment when the Law on Privatization ("Official Gazette" No. 38/01, 18/03, 45/05 and 123/07) came into force. Specifically, the consequences of the revocation of the decisions and actions taken on the basis of these decisions had *ex tunc* effect, that is, it was as if they had never existed, which means that by the time of the adoption of the Law on Privatization, no legally valid action regarding the ownership transformation had been carried out at *Novosti*. Therefore, *Novosti* could be privatized only according to the provisions of the Law on Privatization, because it had not initiated the proceedings of ownership transformation before the adoption of this Law.

However, after the political changes in 2000, *Novosti* continued to operate as a shareholding company, despite the court's judgment and the decisions of the Directorate. The Shareholders' Assembly met and issued decisions in spite of the fact that the share capital had been cancelled.

2. Registration of Cancelled Privatization with the Court Registry

The Extraordinary Shareholders' Assembly Meeting of the company *Novosti ad* held on 12 October 2002 passed a decision on establishing the ownership structure of the Company in the ratio of 70.48% state-owned and 29.52% privately owned capital, and on the issuance of 6739 shares, based on the evaluation of capital made on the basis of the Regulation Amending the Regulation on the Federal Public Institution (SJU) *Borba* (Official Gazette of the FRY No. 12/2001). However, the said Regulation regulated only the process of evaluation of the state-owned assets used by the Company's subsidiaries operating within the SJU *Borba*, and not the privatization process of the SJU *Borba*, or any part thereof. The Regulation also provided for agencies that were to participate in the evaluation of capital value: the authorized appraiser, who is chosen by the Federal Government on the proposal of the Federal Secretariat of Information, then the Commission for the Analysis of Evaluation and the Federal Government.

The evaluation was made by *Proinkom* from Belgrade according to the Regulation. In the evaluation text analyzed by the Council, which

was delivered to us by the Archives of Yugoslavia in the attachment to the Minutes of the meeting of the Federal Government where the acceptance of the evaluation of Novosti was decided, *Novosti* is treated as part of the SJU *Borba*.

The Commission of the Federal Government to review the evaluation made a report on the *Proinkom* Evaluation in July 2002, in which the Government made a proposal for a new organization system of *Borba*. The Commission proposed the establishment of the company *Novosti a.d.* that would include *Sport*, the Agency *Borba* and *TV Novosti*, stating at the same time that "according to the assessment, the state-owned capital in *Vecernje Novosti* is 23.76%". It is unclear what kind of assessment it was, because *Proinkom* did not determine the capital structure of *Novosti* and the stated data corresponds to the amount of the socially-owned capital from the Decision of the Directorate for the Evaluation of Capital, which had been revoked by the court. The Commission also proposed an increase in the state-owned stake in *Novosti* from 23.76% to 29.52%, with an explanation that the company *Novosti a.d,* together with new editorials, would increase its capacities by the use of *Borba's* building which is located on Nikola Pasic Square and Kosovska Street. *Proinkom*, however, did not assess the value of this building, which is registered as state-owned property, so it is not clear how the specified percentage was calculated. The Commission also noted that this "offer" for the change in the ownership structure came from the company *Novosti*. The Federal Government adopted the Commission's Report on the Review of the Evaluation at its 64th meeting held on 15 August 2002 and passed the Decision approving the evaluation.

At the Assembly Meeting of the company *Novosti,* held on 12 October 2002, member of the Supervisory Board Svetlana Vukovic raised some questions related to the *Proinkom* Evaluation. The Minutes of the Assembly Meeting state that the Director of the Company Manojlo Vukotic responded that the member of the Supervisory Board "used the data from the *Proinkom* Agency's Report, whose evaluation was unacceptable for *Novosti*, and which was superseded by the Decision of the Federal Government. Specifically, the initial evaluation was that the entire capital of the Company was owned by the state, and that the percentage of 70.48% share capital was established through negotiations", which Vukotic described as "a great victory for *Novosti*".

In accordance with Article 23d of the Regulation Amending the Regulation on the SJU *Borba* (Official Gazette of the FRY No. 12/2001), the changes made on the basis of the evaluation of the assets or prop-

erty could not be entered in the court register without the explicit consent of the Federal Government. However, the Commercial Court of Belgrade allowed by the Decision V Fi–12252/02 of 31 October 2002 the registration of the NIP Company *Novosti a.d.* Belgrade without the Federal Government's decision giving an approval for the registration of the changes, and without proof that the capital had been paid in. The Court registered the total subscribed and the paid initial capital of 96,613,000 dinars, out of which the paid share capital of natural persons was 68,094,000 dinars, or 70.48%, and the paid share capital of Serbia and Montenegro was 28,519,000 dinars, or 29.52%, although there was no documented evidence that the capital had been paid. The Decision indicates that the registration was made on the basis of the Regulation, which could not be used as the basis for the registration, because the Regulation only prescribed the process of evaluation of the state-owned capital of the SJU *Borba*, and not the privatization process. In order to have the ownership of the capital structure registered, there must be evidence on the basis of which the court must determine exactly by whom, when, how and in what amount the initial capital has been paid. The Court Registry does not have the Federal Government's consent for the registration of the changes, and the Court does not refer to it in its explanation, nor in the evidence of the payment of the capital.

The fact that the distribution of shares to small shareholders was made only two years after the issue of the Decision on the issuance of shares and after the registration of the share capital with the Court Registry proves that no evidence on the payment of the initial capital could have existed either. The share of the small shareholders in this distribution was even changed in relation to that stated at the Court Registry, as the Pension and Disability Insurance Fund shares, which were not shown in the procedure of registration with the Court Registry, were deducted from it, so that the Book of Shareholders was registered with the Central Securities Depository only on 2 July 2004 with the following capital structure: 63.33% of the shares owned by small shareholders, 7.15% of the shares owned by the Pension and Disability Insurance Fund, and 29.52% of the shares owned by Serbia and Montenegro.

The documentation of the registration of the NIP Company *Novosti a.d.* Belgrade with the Commercial Court Registry in 2002 shows that pressure was exerted on judges to make an unlawful registration. Specifically, the registration of a business entity in the register is strictly a formal procedure which prescribes the form and the enclosed docu-

mentation required for the registration of the relevant data. Form 2 includes the data on the amount of subscribed and paid initial capital and the ownership structure, based on the submitted evidence of payment. It is interesting that all the forms Fi 12252/02, dated 31 October 2002, were signed by the registration judge Mirjana Trninic except for Form 2, on which there is no signature. Form 2 is not complete in the dossier documentation, or more precisely its back, which contains a stamp signature of Judge Marina Tomic. It is obvious that there was a problem with the signing of this Form, which clearly indicates that pressure was exerted on judges to register, without the mandatory approvals and without evidence of the payment of capital, an ownership structure that was not in compliance with the Law on Ownership Transformation, the Regulation on Amendments to the Regulation on the SJU *Borba*, the Law on Privatization and the Law on Assets of the Republic of Serbia (Official Gazette No. 53/95, 3/96 – corr. 54/96, 32/97 and 101/2005 – another Law).

After the disputable issues related to the privatization and sale of the shares of the small shareholders of *Novosti* had been made public at the end of 2010, the Company published a text entitled *The Novosti Dossier* on the website of the daily newspaper *Vecernje Novosti*, as well as its interpretation of the events that had become a subject of public interest. Among other things, it was admitted in the *Novosti Dossier* that the registration of the shareholders with the Central Securities Depository and Clearing House was done "on the basis of the Book of Shareholders created in the process of the *Novosti* ownership transformation initiated in 1991 by the issue and sale of shares, and after the distribution of the first round of free shares", based on the ownership transformation process, which was revoked by the Higher Commercial Court's Judgment Urs. No. 84/99 of 16 February 2000. This means that the Newspaper Publishing Company (NIP) *Novosti*, which was 100% socially-owned on the basis of the Court Judgment of 2000, in fact operated as a shareholding company for four years without having a single shareholder, with illegal management and shareholders' representatives in the Shareholders Assembly of the Company. All that time, the Federal Government, the Government of Serbia and the Ministry of Economy were aware that the Company *Novosti* had been usurped by the interest group headed by the director Manojlo Vukotic, who declared themselves as shareholders of the Company despite the court ruling and the Decision of the Directorate, and that the share capital of nonexistent shareholders was registered with the Court Registry.

3. Bid for the Takeover of Shares in 2005

Rather than taking measures to annul the illegal registration, the Ministry responsible for privatization used the illegal situation in *Novosti* in the following years to prevent the takeover of the shares by investors interested in the company.

On 17 May 2005 the business company SENTA HANDELS ANSTALT, based in Liechtenstein, submitted to the Securities Commission a request for approval of the takeover offer NIP *Novosti a.d.* Belgrade. According to the Councils' knowledge it was WAZ company standing behind this offer. While the Commission was deciding on SENTA HANDELS ANSTALTs' request, the Government suddenly opened up the disputable issues of the property relations in *Novosti* that had been known to it for years. Thus, on 1 June 2005 the news agency BETA published the following news: "According to information coming from the Serbian Government, maybe *Novosti* is not a shareholding company. Specifically, the High Commercial Court revoked the privatization of *Novosti* and reverted it to the status of a socially-owned enterprise in January 2000. However, two years later, the then Federal Government adopted a decision according to which the employees became the owners of 70% of the capital and the state became the owner of 30% of the *Novosti* capital."

The next day, the Privatization Committee of the National Assembly addressed the Prime Minister of Serbia with the recommendation that the Government should suspend all activities related to the takeover of the *Novosti* shares until the actual state of the ownership structure and the method and review of the evaluation of its capital were established. On 3 June 2005 *Vecernje Novosti* published an extensive article entitled "Serbia robbed of *Novosti*", in which, among other things, they conveyed the statement by the Chairman of the Privatization Committee, Nikola Novakovic: "I have discovered devastating data, but an encouraging conclusion. The way the registration of the changes was carried out was faulty and deficient, because the court registered the changes rather arbitrarily, referring to the Decision of the Government of the FRY. It cannot even be seen whether an assessment of the capital was made, or who made it." The same article quotes a statement by the Minister of Economy, Predrag Bubalo: "Every other step in the entire procedure from the beginning of the nineties was unlawful, semi-lawful and contestable decisions were made. That was why I have decided to respond. Had I not found it out, I would be sleeping

peacefully and I wouldn't have any questions regarding the privatization of *Novosti*. And now I can sleep even more peacefully because I have warned of the existence of problems. Two days ago I had a meeting with the small shareholders and I suggested to them what I am saying now as well: to wait for the adoption of the new law, to make a majority package of shares and a serious tender. I have concluded, by my professional conscience and position, that we should wait. "

By its Conclusion No. 022–8631/2005–003 of 9 June 2005 the Government of Serbia decided to terminate the Agreement on the Regulation of the Founders' Rights in the Federal Public Institutions and State-Owned Media Companies, which was concluded with the Government of the Republic of Montenegro on 1 February 2005. In the information attached to the Decision, the Government stated that it was found out subsequently, after the signing of the Agreement, that "the ownership structure of the capital of the company NIP *Novosti* ha[d] not been established and it [was] not known what the share of state-owned capital of *Novosti* was, nor what proportion of the capital [could] be privatized" and it referred to the Recommendation of the Privatization Committee of the National Assembly. Following the request of the Republic Public Attorney, the Commercial Court of Belgrade adopted the following provisional measure on 28 June 2005, by which the State Union of Serbia and Montenegro was prohibited to dispose of the *Novosti* shares because of the dispute between Serbia and Montenegro and the Republic of Serbia. Because of the Court Decision, the Securities Commission made, at the 84th meeting held on 20 July 2005, Conclusion No. 4/0–32–1278/8–05, by which it suspended the proceedings initiated at the request of SENTA HANDELS ANSTALT, thus preventing the takeover of the *Novosti* shares.

Four years after the unlawful registration, on 16 February 2006 the Government passed Conclusion No. 464–766/2006 by which it ordered to:

- The Republic Attorney General to register the rights to the immovable property used by *Novosti*, *Borba* and the *Borba* Printing House in favor of the Republic of Serbia;
- The Ministry of Economic Affairs to review the evaluation of the value and the ownership structure of the capital, as well as the title holder of the shares of *Novosti*, *Borba* and the *Borba* Printing House with the aim of determining the share of the state-owned capital in the total capital of these companies; and

– The Ministry of Economy to take measures in the privatization process in order to suspend all the activities related to the registration and issue of shares of the mentioned companies, until the completion of the review.

The Government's Conclusion confirms the information released by BETA on 1 June 2005. In fact, the Government was aware that *Novosti* had not been privatized and that the registration of the state-owned and privately owned share capital was unlawful, that the amount of the state-owned share in the total capital of *Novosti* had never been determined, and that during the registration in 2002 the percentage of the socially-owned share in the *Novosti* capital was actually just copied as it was before the cancellation of the *Novosti* ownership transformation. For this very reason, the Government ordered the Ministry to determine the ownership structure of the Company.

The Government's Conclusion was adopted by applying Article 48 of the Law on Assets Owned by the Republic of Serbia, which prescribes that the Government of Serbia, in agreement with the legal person using assets built or acquired through the participation of the Republic's funds, should determine the share of the state ownership in the assets used by the legal person. In cooperation with the competent ministry, the Property Directorate submits a proposal of the agreement to the legal person. If the agreement is not concluded within a period of six months from the date of its submission, the obligation of the Republic Public Attorney is to submit a request to the Court to determine the ownership rights and the state-owned share.

The procedure that was to be conducted by the Ministry of Commerce in accordance with the Government's Conclusion would not have concealed the fact that *Novosti* had not been privatized either according to the regulations that were applicable in the nineties, or according to the 2001 Law on Privatization. It would have also been determined whether the registration of the shareholding company with the Court Registry had been made without a legal basis, and without a previous procedure in which *Novosti* became a shareholding company. No ownership transformation procedure of *Novosti* was conducted or initiated at the time of the registration in 2002, and the percentage of the socially-owned capital from the Decision of the Directorate for Evaluation of Capital No. 647/98–1–6 from 1998, which was revoked by the Court, was registered with the Court Registry. Therefore, had the Ministry of Economy acted in accordance with the Law and carried out the review ordered by the Government after having established the facts, it would have had to initiate proceedings for the cancellation of

the unlawful registration, and the publicly-owned company *Novosti* would have been privatized by the Privatization Agency in accordance with the Law on Privatization.

In order to have the aforementioned facts concealed, the Ministry of Economy never initiated a review ordered by the Government. Instead of a review, on 21 February 2006 the Ministry passed the Conclusion No. 764/91, by which it ordered the NIP Company *Novosti a.d.* to submit the documentation related to the procedure of the privatization of the Company conducted according to the provisions of the Law on Socially-Owned Capital. The Ministry of Economy stated in the explanation of the Conclusion that it made this order acting in accordance with the Government's Conclusion and pursuant to Article 77 of the Law on Privatization, which stipulates that the Ministry should continue to exercise control and verification of the initiated but uncompleted ownership transformation procedures. However, as all the decisions regarding the ownership transformation and subsequent actions based on them had been revoked by the Court Decision and the Decision of the Directorate for Evaluation of Assets, Article 77 of the Law on Privatization could not be applied in the case of *Novosti* because the Company was not in the process of ownership transformation at the time when the Law on Privatization came into force.

Novosti did not act in accordance with the order of the Ministry, and therefore the Ministry re-issued the same order on 3 April 2006. Even after the repeated order, *Novosti* did not act in accordance with it. At the same time, despite the explicit order of the Government, the Ministry did not take any measures to suspend the activities related to the registration and issue of the *Novosti* shares, so that their shares were offered without any obstruction at the Belgrade Stock Exchange on 21 August 2006.

It is stated in the document entitled *Information on the Status of the Case of the NIP "Novosti" a.d. Belgrade (Chronological Genesis According to the Available Records of the Ministry of Economy)*, which was submitted by the Ministry of Economy at the beginning of November, 2006 to the Privatization Agency, the Shares Fund, the Central Securities Registry, the Securities Commission, the Republic Directorate for Property, the Treasury Directorate of the Ministry of Finance and the Republic Public Attorney, among other things, that, after *Novosti* had failed to act in accordance with Ministry's order, the information in the documents of the Ministry of Economy regarding the capital structure of *Novosti* differed significantly from the information recorded in the Decision of the Commercial Court in Belgrade and from the data

of the Central Registry. Despite this knowledge, the Ministry did not take any steps to carry out the order of the Government of Serbia of 16 February 2006, but instead only forwarded the Information on the unlawful actions to the aforementioned state agencies without any additional instructions regarding the measures to be taken. By the time this Information was forwarded, in November 2006, the majority package of the *Novosti* shares had already been sold through the Belgrade Stock Exchange.

The actions of the Ministry of Economy clearly lead to suspicion of their complicity with the interest group headed by the director of *Novosti* Manojlo Vukotic and the financially powerful individuals who made an agreement with Vukotic to take over the Company. Specifically, the Ministry first used the unlawful registration of *Novosti* with the Court Registry to prevent the implementation of the takeover bid submitted by SENTA HANDELS ANSTALT, and then, by failing to act in accordance with the Government's Conclusion of 16 February, made it possible that the shares issued on the basis of unlawful registration with the Court Registry could be sold at the Stock Exchange.

4. Sale of Shares in 2006

At the Shareholders Meeting of the company *Novosti* held on 27 May 2006, which was attended by the representative of the state-owned capital Srdjan Djuric, then director of the Government's Office for Media Relations and a member of the ruling Democratic Party of Serbia, the director of *Novosti* Manojlo Vukotic informed the shareholders that he and "a team of associates" had come "to the commitment" that the shares of the company should "go to the stock exchange" and that they had "found some good, rich and experienced Serbian businessmen willing to buy the shares". Vukotic refused to answer the shareholders' question as to which businessmen those were, but he said: "I am fully convinced of their good intentions, their knowledge, their ambition and, if my word is worth anything, I guarantee for them. I stand behind them or in front of them."

On 21 August *Novosti* offered its shares on the Belgrade Stock Exchange. It was stated in the Prospectus for the first trading of the shares on the Stock Exchange, signed by the director of the Company Manojlo Vukotic, that the issuer had the right to use the 6,000-m2 offices, but that proceedings establishing the property rights were being conducted before the Commercial Court. This information did not

match the information in the Real Estate Register at the time, in which NIP *Borba a.d.* Belgrade was registered as the user, and the dispute initiated by *Novosti* against *Borba* and the Republic of Serbia before the Commercial Court in Belgrade in order to verify the co-ownership of *Novosti* of the building on Kosovska Street has not been ended so far. A prospectus is an essential source of information for the shareholders and prospective investors, on the basis of which decisions are made regarding investing in the shares and other securities issued by a company. The Law on the Securities Market prescribes heavy fines both for the legal and the responsible person in the legal person for presentation of false information in a prospectus as a public document.

Within a period of eight days from the date of taking the shares to the Stock Exchange, almost all small shareholders of *Novosti* sold their shares at a price of 289,488 dinars per share, or around 3,400 euros. The shares of the Shares Fund and the Pension and Disability Security Fund were not sold. Only on 3 October 2006 the Privatization Agency submitted to the Shares Fund the Decision No. 7841/06 on the Method of Sale of Shares of the Company NIP *Novosti* on the Stock Exchange, with an order to sell 482 shares belonging to the Pension and Disability Insurance Fund. However, on 1 November the Ministry of Economy sent an opinion to the Shares Fund and the Privatization Agency that the sale of the shares of the Pension and Disability Insurance Fund should be suspended, and that the sale of the shares owned by the Republic of Serbia in *Novosti* should not be initiated until the completion of all the proceedings conducted before the competent institutions.

The shares sold in August 2006 by the small shareholders of *Novosti* were bought by the companies STADLUX REALESTATE d.o.o. Belgrade and ARDOS HOLDING GmbH Austria. At the time of the sale, virtually all relevant media in Serbia reported that Milan Beko was behind the buyers of the *Novosti* shares, but the Securities Commission did not respond to this information.

Actions by the Securities Commission

As both STADLUX and ARDOS exceeded 25% of the ownership and failed to inform the Stock Exchange and the Securities Commission about it, and did not submit a bid for the takeover, whereby they violated Article 6 of the Law on the Takeover of Joint Stock Companies (Official Gazette No. 46/2006 and 107/2009), the Securities Commission initiated the procedure of supervision and control of the trading

in the shares of the NIP Company *Novosti a.d.* Belgrade. Having established the existence of irregularities, the Commission took the following steps:

- It issued a decision by which STADLUX was ordered to submit to the Commission an application for approval to publish the bid for the takeover of the *Novosti* shares in the manner and under the conditions prescribed by the Law on the Takeover of Joint Stock Companies, or if it did not have necessary funds to conduct the takeover procedure or if the conditions for publishing the bid for the takeover had not been fulfilled in accordance with the Law, to sell an appropriate number of the *Novosti* shares on an organized market within a period of three months from the date of receipt of the Decision, so that the number of its shares would not exceed 25% of the voting shares. It was established by the Commission's Decision that STADLUX did not have the voting right on 558 acquired shares in *Novosti* as of the issuance of the Decision. However, before the delivery of the Decision, STADLUX had reduced their percentage to below 25%, and consequently the Decision was withdrawn.
- As ARDOS had acquired 173 voting shares, exceeding the regulatory threshold of 25%, the Commission issued the same decision as in the case of STADLUX, but since the company ARDOS had sold some of the *Novosti* shares and thereby reduced the percentage to below 25%, the Commission withdrew its decision. The Commission also ordered the authorized person in ARDOS to submit a statement regarding its concerted action with the other buyers, but ARDOS did not carry out this order. The Commission issued a conclusion by which the proceedings were terminated and a decision to reopen the supervision should it have evidence of a concerted action of the buyers of the *Novosti* shares.
- The Commission notified *Novosti* that, pursuant to Article 37 of the Law on the Takeover of Joint Stock Companies, the companies STADLUX REAL ESTATE and HOLDING ARDOS did not have the voting right on the basis of the acquired shares exceeding 25%, and that the body which called an extraordinary shareholders meeting scheduled for 22 September 2006 should be informed about it, and that *Novosti* should inform the Commission if these shareholders had voted at the extraordinary meeting on the basis of the acquired shares to

which they were not entitled, and if such votes were decisive for the adoption of the proposed decisions, but there has been no feedback regarding it.

After STADLUX and ARDOS had sold shares exceeding the ownership of 25%, STADLUX sold all their *Novosti* shares, so that the following ownership structure was established: ARDOS HOLDING had 24.89% of the shares, TRIMAX INVESTMENTS had 24.99%, KARAMAT HOLDINGS 12.55%, the Republic of Serbia 29.52%, the Pension and Disability Insurance Fund 7.15% and other shareholders had 0.90%.

The way the small shareholders' *Novosti* shares were purchased clearly suggests that it was a covert takeover. At the moment when the *Novosti* shares were offered on the organized market, the buyer was aware that it was not possible to apply for approval of the takeover bid because it did not fulfill the basic requirement from Article 1, Paragraph 3, of the Law on the Takeover of Joint Stock Companies, because the shares had been traded on an organized market for three months before the publication of the notice of intent for a takeover. Besides, the temporary measure of the Commercial Court of Belgrade of 28 June 2005, which prohibited the disposal of *Novosti* shares owned by Serbia and Montenegro, was still in effect. It is obvious that the buyer knowingly made the decision to carry out the takeover in an unlawful manner, and exceeded the prescribed threshold of the 25% stake by buying shares on the stock exchange, in order to be able to take control of *Novosti* by subsequent sale of the surplus shares to a related person. Also, the findings of the supervision and control clearly show that the Securities Commission was aware that related persons, both individually and jointly, acquired more than 25% of votes in *Novosti*, because of which an application for approval of the takeover bid should have been submitted, but the preliminary requirements had not been fulfilled for it, and it could not be approved either within the three months' time because of the temporary measure imposed by the Commercial Court of Belgrade.

To the Anti-Corruption Council's question as to whether *Citadel Securities* had informed the Securities Commission that the buyers it represented were related persons, sent on 19 July 2010, the Commission replied on 20 August that it "did not have any information nor had it been informed by any third person about a possible connection between some of the buyers of the subject shares". On 30 July 2010 the Council requested the Commission to provide it copies of decisions and other acts related to the findings in the process of control and su-

pervision related to the trading of the *Novosti* shares, which we have not received so far. As the Commission did not submit the requested documents within the statutory deadline, the Council appealed to the Commissioner for Information of Public Importance. Following the decision of the Commissioner, on 26 November 2010 the Commission sent to the Council a letter "on available information", stating the measures taken by the Commission in exercising the control of the trading in the *Novosti* shares, but it did not deliver the required copies of relevant decisions, conclusions and notifications, which it had issued and delivered to the controlled parties and to *Novosti*. On 25 December the Council reiterated its request, at the same time also requesting information related to other allegations that had been made public in the meantime.

Appearing on the TV B92 show *Izmedju redova* (*Between the Lines*) on 21 November 2010, Milan Beko confirmed that the three companies through which they purchased the *Novosti* shares belonged to him: "There has been no doubt about it since the beginning," said Beko. On 27 November 2010 Vesna Vujic from the Securities Commission stated that, after Beko's appearance on TV B92, the Commission requested from his companies "an official explanation of whether they were connected", pointing out that the Commission had examined the connection between the owners of *Novosti* four years before as well, but it "had never received an answer". This statement is in stark contradiction with the information the Securities Commission provided to the Anti-Corruption Council on 20 August 2010.

In a repeated request for delivery of documentation regarding the control of the purchase of the *Novosti* shares of 25 December, the Anti-Corruption Council also asked the Commission if it, at the time of the control, had documentation indicating that the buyers of the *Novosti* shares were related persons behind which was Milan Beko, and what legally prescribed actions they took after Milan Beko's public confession that he is the owner of more than 60% of the *Novosti* shares. By the Decision No. 1/0–06–442/24–10 of 14 February 2011, the Commission refused the Council's request for access to information of public interest, on the grounds that the police had opened preliminary criminal proceedings relating to the acquisition of the *Novosti* shares and that such information was considered an official secret in the light of Article 239, Paragraph 2, of the Law on the Securities Market and Other Financial Instruments (Official Gazette of the Republic of Serbia No. 47/2006). The Council filed an appeal with the Commissioner for Information of Public Importance, but it is still pending.

The Chairman of the Securities Commission Milko Stimac announced on the national RTV *Pink* news on 24 February 2011 that "this body will complete the control of the ownership of the company *Novosti* by mid-March and request that one of the three companies, two based in Austria and one from Cyprus, which have a majority stake, publish the binding bid for acquisition of the remaining shares". Mr. Stimac also said "the Commission will persist in verifying the ownership in the company, because no equity buyer can remain hidden". Despite repeated announcements on several occasions, the Commission has not carried out the control of the ownership of the company *Novosti*.

Unlike the company KARAMAT HOLDINGS, where difficulties may arise during the control of the ownership as it was established at an "off-shore" destination, it can be simply established by researching publicly available information from relevant registers that the companies ARDOS and TRIMAX are related in terms of Article 4, Paragraph 2 and 3 of the Law on the Takeover of Joint Stock Companies, as they are under the control of the company BICOS Beteiligungen Gesellschaft GmbH, based in Austria, and Dr. Gottfried Wieser. According to the statement from the relevant Commercial Register:

- The only member of ARDOS is BICOS, with 100% stake in the founding capital, and the only registered agent of ARDOS is Dr. Gottfried Wieser;
- The only member of the company ABISCO Verwaltungen GmbH, based in Austria, is TRIMAX, with 100% interest in the founding capital;
- The only member of ABISCO is BICOS, with 100% stake in the founding capital, while Gottfried Wieser is the only registered agent of ABISCO;
- The only registered agent of BICOS, and the majority shareholder of the Company, with 99.175% share in the capital, is Dr. Gottfried Wieser.

Thus, through his ownership of shares in BICOS, Dr. Gottfried Wieser owns both ARDOS and TRIMAX, and thereby has direct influence on ARDOS and BICOS, because he is the only registered agent of these companies, and indirect influence on TRIMAX, as he is the only registered agent of the owner of TRIMAX. In terms of Article 4 of the Law on the Takeover of Joint Stock Companies, the companies ARDOS and TRIMAX are considered to be parties that operate together and that are subject to the obligation to publish their takeover bids. As to

the company ARDOS, in 2006 the Commission issued a Conclusion by which it stopped the proceedings instituted *ex officio* in relation to the acquisition of the *Novosti* shares, and a decision to reopen the supervision procedure should the Commission have evidence that the buyers acted in concert. The Anti-Corruption Council acquired information on the joint action of ARDOS and TRIMAX by examining the publicly available information of the relevant register of the Republic of Austria, so the statements by the officials of the Securities Commission, which suggest that this institution, even after almost five years, still cannot carry out an audit of the ownership in the company *Novosti*, sound extremely unconvincing.

Actions by the Commission for Protection of Competition

On 19 January 2009 the Austrian company OST Holding Sudosteuropa GmbH, which is part of the WAZ Group, submitted to the Commission for Protection of Competition an application for approval of concentration, regarding Sudosteuropa OST Holding's intentions to acquire indirect control of the NIP Company *Novosti a.d.* by gaining direct control over the three shareholders of *Novosti*: TRIMAX, ARDOS and KARAMAT. The applicant proposed that the Commission approve the intended concentration in summary proceedings and without providing any special conditions and without the hearing of the parties pursuant to Article 23 of Law on Protection of Competition (Official Herald of the Republic of Serbia No. 79/05). Since 19 January 2009, the Commission for the Protection of Competition has taken the following steps regarding the OST Holding's application:

- It requested on 9 February 2009 additional documentation and explanation of certain information provided in the application. On 13 and 19 February 2009 OST Holding amended the application providing requested documents and information. So far the Commission has not made any decision, or invited the applicant to amend the application.
- Article 23, Paragraph 5 of the Law on Competition provides that parties to the concentration are obliged to stop the implementation of the concentration "until the expiry of a period of four months from the date of the application". Considering the fact that after 19 February the Commission did not request any further information, or amendments, on 2 July 2009 OST Holding addressed it with a submission reading: "In our understanding the application of 19 February 2009 was duly

filed and completed in accordance with Article 23, Paragraph 5 of the Law on Protection of Competition. The consequence of this is that the ban on OST Holding to enforce the relevant concentration and thus gain control over *Novosti* has expired as of 19 June 2009." So far the Commission has not responded to this submission.

- Meanwhile, the new Law on Protection of Competition was adopted (Official Herald of the Republic of Serbia No. 51/09). The application of the Law began on 1 November 2009, and Article 74 stipulates that the proceedings commenced before the effective date of the new Law should be conducted according to the regulations by which they were initiated. On 25 January 2010 OST Holding submitted to the Commission an updated application regarding the concentration on the basis of Article 61 of the new Law, and the Commission responded to it on 26 February 2010, requesting certain additional information as soon as possible. The legal representative of OST Holding submitted the requested information on March 3, and since then the Commission has again remained silent.
- On 6 May 2010 OST Holding addressed the Commission requesting an explanation as to whether the new Law on Protection of Competition and Article 65, Paragraph 2 of the Law applied to it, according to which it is considered that the concentration is approved if the Commission does not issue a decision within 30 days from the date of the application. OST Holding submitted the same request to the Commission on 23 June and then again on 28 June 2010. On June 30 the Commission delivered its Opinion to the applicant that, in accordance with Article 74 of the Law, the same regulations by which the proceedings were initiated were applied to the concrete case.
- On 6 July 2010 the Commission requested the OST Holding to provide information as to whether the ownership of the Novosti shares had been changed in the meantime.

In other words, the procedure OST Holding is conducting before the Commission for Protection of Competition has lasted more than two years, from the submission of the application on 19 January 2009 to date, with no chance of its completion.

Owing to the actions of the Securities Commission and the Commission for Protection of Competition, the related companies, control-

led by Milan Beko according to his own admission, have for almost five years had a majority ownership in the company *Novosti*, which they acquired in August 2006 by violating the Law on the Takeover of Joint Stock Companies, the Law on Privatization and the Law on Assets Owned by the Republic of Serbia.

5. Conclusions and Recommendations

The Anti-Corruption Council has gathered and analyzed extensive documentation which shows that over a period of ten years the state institutions have continuously issued unlawful decisions in the privatization of *Novosti*, which have been detrimental to the Republic of Serbia, and in favour of the interest group which usurped the company in 2000 and in favour of the tycoons with whom this group had conformed in order to acquire a majority stake. It should be noted that the usurpation of *Novosti* has not only caused damage to the Republic of Serbia, but also to the other employees of *Novosti* who were entitled to free shares of the Company in the privatization process. Consequently, on 22 January 2008 a group of 26 workers and former workers of *Novosti* filed a lawsuit with the First Municipal Court of Belgrade against Serbia, the NIP Company *Novosti a.d.* and Manojlo Vukotic for damages, as they have been denied their right to free shares under the Law on Privatization because of the "continuation" of the ownership transformation of the Company.

In 2000 *Novosti* was a 100% socially-owned company. The process of ownership transformation was not initiated in it and it was not privatized according to the Law on Privatization, nor did the Ministry responsible for privatization initiate this process after 2001. All relevant authorities were aware that the registration of the shareholding company with the Court Registry in 2002 was unlawful because no legally prescribed process of privatization was conducted. Though the Government of Serbia, following the perceived illegality, ordered the Ministry of Economy in 2006 to review its ownership structure and take measures to suspend the registration and issue of the *Novosti* shares, the Ministry did not do so. Had the review been made and had the process of making an agreement been opened as foreseen by the Law on Assets Owned by the Republic of Serbia, it would have been determined that the state-owned share in the total capital of *Novosti* was much higher than was registered, because the state-owned build-

ing at 20–26 Kosovska Street was not included in the evaluation of the capital.

Novosti claims the right to the building on Kosovska Street, which is clear from the fact that it filed a lawsuit with the Commercial Court of Belgrade against the Republic of Serbia in order to verify its co-ownership. Therefore, no ownership structure of *Novosti* could have been determined without an assessment of this facility, and had the Ministry of Economy made it during the review ordered by the Government, the majority of the *Novosti* shares would have been sold by the Republic of Serbia. In that case, however, the sale of the shares would have been followed up by the public quite differently – as privatization of state-owned capital for which the Ministry of Economy and the Shares Fund would have been responsible, and not as a private transaction between small shareholders and three unidentified foreign companies. However, by avoiding the review of the evaluation, or failure to act on the order of the Government, the Ministry allowed the ownership structure of *Novosti* to remain as it had been registered in 2002 with the Court Registry, and after that, to sell on the Belgrade Stock Exchange the majority package of shares owned by small shareholders, acquired by usurpation of the state ownership, and without even raising the issue of concentration, because the *off-shore* companies owned by Milan Beko did not operate in the field of information and advertising. The manner of sale, which was enabled by the Ministry of Economy through its failure to act, actually led to the situation where the establishment of control over the biggest-selling daily newspaper in Serbia took place as if it was a transaction of no public interest. Decisions that were then made by the Securities Commission and the Commission for Protection of Competition enabled Milan Beko to unlawfully control one of the most influential and profitable information companies in the country for nearly five years.

It would be necessary to analyze how so many irregularities occurred by which the group of people led by Manojlo Vukotic was allowed to register in relevant commercial registers changes that never happened, and to then realize his agreement with Milan Beko to sell the illegally obtained assets on the securities market. In other words, how was it possible that, in the period after 5 October 2000, when privatization was singled out as a process on whose success the implementation of democratic reforms critically depended, such a valuable and important company as the publishing house *Novosti* was transformed from a socially-owned to a to private company entirely outside the law and the institutions that regulate privatization and the capital market?

First of all it is necessary to analyze, on the basis of facts, mechanisms that made it possible for state institutions to act so drastically in favour of the interests of powerful individuals, and not in accordance with the law, and to consider with utmost care the facts that point to corruption in the actions of all those involved in the privatization and sale of the *Novosti* shares, and to take appropriate steps to establish their accountability.

It is also important that the Government prevent further damage to the Republic of Serbia in the privatization of the remaining parts of the former SJU *Borba*, which are controlled by the structures that are behind the unlawful privatization and sale of the *Novosti* shares, which primarily refers to the Printing House *Borba*.

By the application of the Law on Payment of Wages (Official Gazette of the SFRY No. 37/90 and 84/90), the employees of the Graphic Printing House *Borba a.d.* acquired the right to the ownership of 20.58% of the total capital of the Printing House on the basis of the final judgment of the First District Court of Belgrade P1–337/97 of 19 May 1997, and on the basis of the final judgments of the Commercial Court of Belgrade XIV-P–3998/01 of 4 March 2002. On 4 March 2011 the Anti-Corruption Council addressed the Privatization Agency with a request to provide information about the status of the privatization of the remaining 79.42% of the share capital of the Printing House *Borba* that belongs to the Republic of Serbia. On March 22 the Agency replied that no initiative for the privatization of the Printing House had been taken yet, which is an action which starts the privatization process, and which may be taken according to the Law on Privatization by a body of the company to be privatized, by interested buyers, or by the Ministry responsible for privatization. In its response to the Council the Agency also stated that the Association of the Minority Shareholders of the Printing House addressed it on several occasions regarding the initiation of the privatization process, and that the Agency conveyed that information to the Ministry responsible for privatization, which responded that it would forward the material to the Government for consideration if the conditions for taking the initiative were fulfilled.

In other words, for the past ten years no action foreseen by law has been taken concerning the privatization of the Printing House *Borba*.

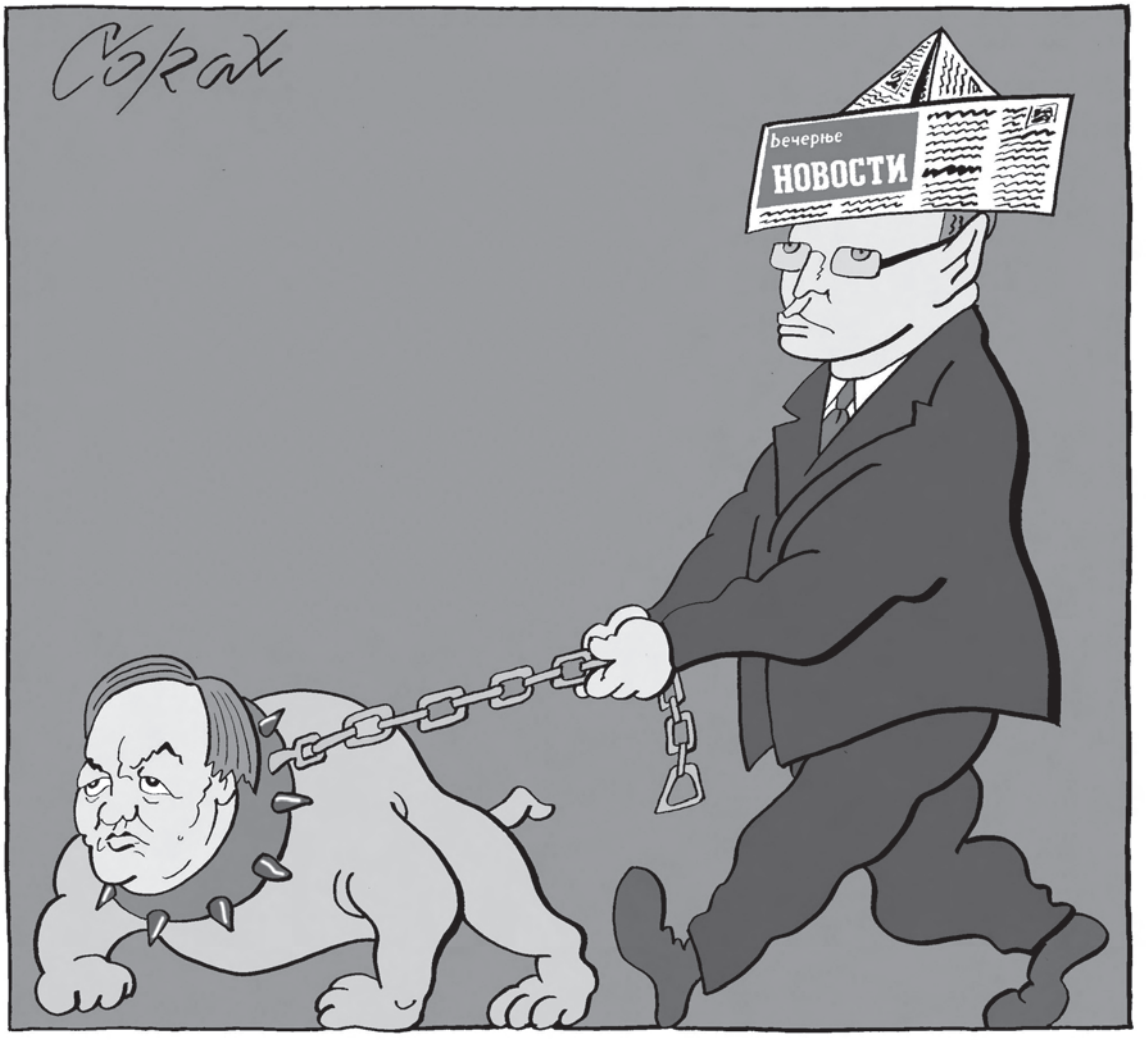
Meanwhile, on 24 April 2002 the Graphic Printing House *Borba* concluded an agreement with the company *Novosti a.d.* on a joint investment, whose subject is the procurement of new printing equipment.

The Printing House *Borba* and the company *Novosti* would each contribute 50% of the required funds for the procurement of equipment. However, this equipment never entered the Printing House *Borba*; but, on the same day when the agreement on joint investment was signed, *Novosti* and the Printing House *Borba* set up a joint venture company Printing House *Novosti d.o.o*, including the new printing equipment in the founding capital of this company, in which *Borba* and the company *Novosti* own 50% of the capital each. The Printing House *Novosti d.o.o.* was registered at Kosovska Street 26, that is, at the location of the Printing House *Borba*. The Printing House *Novosti* has no employees or premises, but through this company the employees of *Novosti* close to its director Manojlo Vukotic run the business operation of the Printing House *Borba*. Establishing the joint venture company limited actually enabled *Novosti* and Vukotic to carry out a "spontaneous privatization" of the Printing House *Borba* and to take over control of the printing house, its operations, and the business premises on Kosovska Street that this company used. The failure of the ministry responsible for privatization and its ignoring the proposals of small shareholders to have the Printing House *Borba* privatized fully complied with the interests of *Novosti*, and Milan Beko and Manojlo Vukotic.

Considering the fact that the subject of privatization of the Printing House *Borba* was state-owned and socially-owned capital, we propose that the Government initiate as soon as possible the cancellation of the harmful contracts with the company *Novosti* and to urgently initiate the procedure for privatization of the Printing House *Borba*; and furthermore, that the Ministry of Economy and Regional Development request a report as to why nothing has been done regarding the privatization of the Printing House *Borba* over the past ten years, despite warnings by the small shareholders that the company was under the threat of a "spontaneous privatization".

Belgrade,
May 17, 2011

Yours faithfully,
President
Mrs. Verica Barać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НОВОСТИ

REPORT ON PRESSURES ON & CONTROL OF MEDIA IN SERBIA

The Anti-Corruption Council has gathered data on the basis of which it can be concluded that the media in Serbia are exposed to strong political pressure and, therefore, a full control has been established over them. There is no longer a medium from which the public can get complete and objective information because, under strong pressure from political circles, the media pass over certain events in silence or report on them selectively and partially.

As the media freedom in Serbia has been jeopardized and as there is no fight against corruption without free media, over the previous months the Anti-Corruption Council has requested from the 50 most significant government bodies in Serbia documentation about all forms of cooperation with media, public-relations agencies, marketing agencies, production companies and other media subjects in the period from January 2008 until the end of June 2010, in order to find out the methods by which the state bodies exercise their influence on the media. The analysis covered all the ministries of the Serbian Government, certain state-owned companies, some city utility companies, agencies and other government bodies. The Council has also analyzed the formal ownership structure of the biggest media in Serbia.

On the basis of extensive documentation, the Anti-Corruption Council has made a detailed analysis of media problems in Serbia and has proposed measures for overcoming them. Our intention was to present to the public as many data as possible, together with precise and relevant conclusions and, therefore, we forwarded the draft of this Report, while we were still working on it, to many institutions, organizations and associations whose activities are connected with the media. Thus, among other things, we sent the draft Report to the Media Department of the OSCE Mission to Serbia, to the RTS Management Board chairman, Mr. Slobodan Markovic, and to the professor of the

Faculty of Political Sciences in Belgrade, Dr. Snjezana Milivojevic. The Council has taken into consideration all the relevant remarks regarding the Report and has made corrections in the final wording of this document.

Three basic problems of media in Serbia

One of the most important tasks in fighting corruption is to define clearly the problem of corruption in the public and, therefore, there is no real fight against corruption without the media. Corruption in the very media makes objective informing of the public ill-advised and the public supervision of social activities impossible. When the control over the media by state institutions is stronger than the control the media should have, when the interests of the hidden media owners do not coincide with the interests of the public; when the interests of individuals are realized at the expense of the public interest, which should be protected by the Government, then we have the relativization of the problem of corruption in society.

The Anti-Corruption Council receives a significant number of complaints from citizens and organizations about the work of the media in Serbia, about their being closed due to problems of corruption and their being too connected with the ruling political and economic elites. The Anti-Corruption Council itself has also encountered large problems in addressing the public so far, trying to present examples of law violations by state bodies and elected officials, as well as possible sources of major (systemic) corruption.

International institutions have also noted large problems encountered by the media in Serbia. Thus concern was expressed by the EU Parliament's Resolution on the European Integration Process of Serbia B7–0021/2011, adopted on 19 January this year[1], because of the Government's attempt to control the work of the media, and drew attention to the ownership concentration and lack of transparency in the media ownership structure. The participants of the annual meeting of the European Federation of Journalists, held in June this year in Belgrade, stated that most of the media workers have very low wages and that they are exposed to pressures from different formal and informal centers of power. "How can a journalist be free if he dares not ask what sal-

[1] http://www.europarl.europa.eu/sides/getDoc.do?type=MOTION&reference=B7-2011-0021&format=XML&language=EN

ary he gets?" "Journalists in Serbia have been pauperized, humiliated, silenced and scared" is one of the judgments that could be heard at the Conference of the European Federation of Journalists.

This description of the position of journalists in Serbia is well illustrated by a recent example when a group of journalists whose reporting was not in accordance with the standard of the existing editorial concept were assigned to the positions of assistant journalists and assistant photographers, with salaries of half the amount. Those who did not accept this proposal lost their jobs. Particularly worrying here is the fact that none of the journalists wrote a complaint under their own names or initiated proceedings for the protection of their own rights.

While analyzing the extensive documentation, the Anti-Corruption Council perceived three major problems with the media:

1. **lack of transparency in media ownership;**
2. **economic influence of state institutions on the work of the media through different types of budget payments;**
3. **the problem of RTS, which, instead of being a public service, has the role of the service of political parties and ruling elites, and the consequence of all this is that media are closed due to numerous problems encountered in Serbia, including the problem of corruption.**

The Council has found out that among the 30 most significant analyzed media in Serbia (12 daily papers, seven weeklies, six TV stations and five radio stations), as many as 18 do not have sufficiently transparent ownership, and their real owners are not known to the domestic public. The reason for this is primarily the presence of off-shore companies in the media ownership structure, whose primary purpose is to hide the real media owners and to conceal the interests of such media from the public in this way.

The state institutions in Serbia spend huge budget funds for advertising and promotion, whereby they make their personal and party promotion, which at the annual level exceeds 15m euros on a sample of the 50 most significant institutions. *Telekom Serbia*, the Ministry of Environment and Spatial Planning, the Ministry of Health and the Ministry of Agriculture, Forestry and Water Management have paid the biggest amounts of money to the media and, therefore, it is almost impossible to find an analytical text or an investigative approach by journalists when reporting on the work of these institutions.

Besides the above-mentioned amount of 15m euros, depending on the source, the media receive an additional 21 to 25m euros through public tenders. Specifically, the data on this are incomplete and, according to the Media Study of the Ministry of Culture[2], this amount was 25m euros in 2010, while certain documents, also from the Ministry of Culture and the Provincial Secretariat, show that the amount was approximately 21.5 m euros. In any case, if you compare it with the total advertising market figure of about 160m euros, it can be concluded that approximately one quarter of their income comes from the state institutions.

Public relations agencies, marketing and production agencies, mainly owned by party activists and persons related to them, play a special role in funding media and keeping them in economic dependence and uncertainty.

The state authorities exercise special influence through RTS which, instead of being a public service to the citizens, is a service of political structures and productions which are closely connected with top officials of the parties in power. During the work on this Report, we encountered problems particularly with the part related to the public service, because the RTS management has been refusing for months to deliver the documentation requested by the Anti-Corruption Council in accordance with the Law on Free Access to Information of Public Importance. The Council has not yet received the requested documentation.

Because of all the above stated, the media in Serbia have lost their primary and important role to inform citizens about things important for their lives, as well as the role the media have in raising awareness of a problem. Nowadays, the media owners and politicians use media exclusively as a means for the creation of public opinion for the purpose of achieving the most favourable rating and election results of political parties, and also for making certain individuals' personal profits. Consequently there is no critical approach to the work of the state authorities in most of the media, and it is impossible to find investigative journalistic texts and contributions in the media, except in rare cases when it suits a part of a party or business elite.

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[2] Media Study, Ministry of Culture, http://www.kultura.gov.rs/dokumenti/SRPSKA-VERZIJA-KONACNA.doc, 79 pages.

1. Non-transparent ownership structure of the media

Though the media-related laws in Serbia and the international recommendations and conventions foresee transparency of the media ownership structure and speak about the need of establishing the pluralism of media and prevention of forbidden media concentration, the public does not have complete information about the media owners in Serbia. The Broadcasting Law (Article 41) specifies that a domestic legal person, established by foreign legal persons registered in countries where, according to the domestic regulations of those countries, it is not allowed or it is not possible to establish the origin of the founding capital, cannot take part in a tender for broadcasting a programme. In spite of such a legal provision, there is a great number of media in Serbia whose owners originate exactly from such countries.

Furthermore, the Law on Public Information and Broadcasting (Article 7) stipulates that all forms of monopoly in the area of public information are forbidden for the purpose of protecting the free competition principle. Nobody can have a monopoly in foundation and distribution of public media, or a monopoly in publishing ideas, information and opinion in a public media. Likewise, the CoE Recommendation No. R (94) 13 on Measures to Promote Media Transparency recommends to the member states that, through the inclusion of an adequate legal framework, they enable the public to access the basic information on media so that they could form their value judgment as regards the information, ideas and opinions presented by a concrete media. The legal regulation of the European Union also has a series of recommendations promoting media pluralism, where the issue of transparent capital in the media is essential for the exercise of this principle. However, none of these principles have been applied in practice.

The European Parliament's Resolution[3], by which the PMs expressed their particular concern because the Government has been trying to control the work of the media, and because of the controversies with the privatization of *Vecernje Novosti*, is a proof that Serbia has a serious problem regarding the above stated. Among other things, the European Parliament noted the exceptional significance of the existence of strong and independent media for a democratic society and called for taking steps to ensure their independence from political and other

[3] http://www.europarl.europa.eu/sides/getDoc.do?type=MOTION&reference=B7-2011-0021&format=XML&language=EN

influences. The Resolution particularly drew attention to the ownership concentration and lack of transparency in the media sector.

In spite of the existence of these clear guidelines, out of the 30 most significant media, including 12 daily papers, seven weeklies, six TV and five radio stations with national coverage, the Council found out that there were **even 18 media** in the period from 2008 to 2010 whose real owners were not formally known. It is disappointing that the Public Media Register with the Business Registers Agency of Serbia has not offered a minimum of information on the real media owners, but only information which company formally published certain newspapers or broadcast a programme. The Republic Broadcasting Agency hasn't published data on the ownership of the electronic media for years. Recently, on 21 July 2011, on the RBA web site has been published the graphic representation of the structure of the radio and TV stations with national coverage. Besides the available information about the owners on the Business Register Agency, the representation of RBA provides the information about the owners of foreign legal persons, which participate in ownership of the domestic media. This information does not provide the transparency of the ownership because instead of names of the real owners they published the names of the lawyers who represent the companies. For example, on the RBA web site we found the information that the co-owner of the TV Avala is the company Greenberg invest GmbH, registered in Vienna, owned by Werner Johannes Krauss, a lawyer from Vienna. Greenberg invest owned 48,41 percent of the shares of TV Avala, the public considers that these shares belong to Zeljko Mitrovic, the owner of TV Pink, therefore the RBA did not give an answer who really controls TV Avala.

Out of 11 broadcasters with the national coverage, nine of them do not have transparent ownership. The fact that the interests of the concealed media owners hide behind their non-transparent ownership speaks best about the current media scene in Serbia. Therefore, it is a serious question how much the media, which hide their owner as their greatest secret, are ready to publish true and objective information.

Off-shore companies as media owners

The presence of off-shore companies is characteristic in the media ownership structure, and their primary goal is to conceal their real owners. Thus *TV Prva, RTV, B92, Radio Index* and *Radio Roadstar*, all with national coverage, and also the print media, such as *Vecernje*

Novosti and *Press*, are directly owned by companies registered in Cyprus, while *TV Avala* and the weekly *Standard* are owned by unknown owners from Austria. The biggest problem with the media that have off-shore companies in their ownership structure is the impossibility to identify their owners, which is contrary to the Broadcasting Law applicable to electronic media and contrary to the Law on Public Information and Broadcasting.

These are most frequently shell companies which do not have a classic infrastructure in the country of their origin. The owner is sometimes a natural person from Serbia, and sometimes the owner of a Cyprus company is hiding in the network of other companies established all over the world. Besides, if you register an off-shore company in one of the tax havens, it is almost impossible to find out the identity of the ultimate owner because instead of his name you can possibly come across the name of the Law Office representing that company. Therefore, it is very difficult to follow such trails and find out what interests are intersecting through such media. Besides hiding behind off-shore companies, the actual owners often hide behind domestic companies as well, which are mainly owned by businessmen or politicians.

- **Vecernje Novosti**

Vecernje Novosti is the best example of non-transparent ownership among domestic media, and also of an unlawful takeover by powerful businessmen, what was also noted and particularly criticized by EU MPs.

The majority package of the *Vecernji Novosti* shares is owned by two Austrian companies – *Trimax Investments* (24.99 percent) and *Ardos Holding* (24.90 percent), and by the Cypriot company – *Karamat* (12.55 percent), whose actual owners have been formally unknown for a long time. Certain details on this acquisition were disclosed to the public last year when the German Media Group WAZ published some controversial information about its ownership. Until then there had been only unofficial information, used by the domestic big business owners to hide behind the capital of these off-shore companies.

Milan Beko himself confirmed his ownership of *Novosti* when he was hosted on the TV B92 Programme *Between the Lines* (*Izmedju redova*) in November 2010, by saying that it had never been disputed that he was the owner of the companies *Ardos*, *Trimax* and *Karamat*, and that he was the owner of 62.4 percent of the *Vecernje Novosti* shares. Thereby Beko confirmed that he had bought the said shares unlawfully

and that he has been holding them illegally since 2006 owing to the institutions which have enabled it, because these companies are related legal entities. Specifically, according to the Law on Takeover of Joint Stock Companies, related legal entities can buy on the stock exchange up to 25 percent of shares, while it is mandatory to publish a tender for the takeover of a bigger capital share, inform the Central Securities Register, the Securities Commission and the joint stock company *Novosti*, which has never been done.

Even after the public admission by Milan Beko that the mentioned companies belonged to him, the Securities Commission took seven months to formally establish this fact.

➢ **Press**

A half of the daily newspaper *Press* is owned by a company registered in Cyprus, *Amber Press Ltd*. from Limassol. It is not known who is behind this company, and so far it has only been speculated who the owner of Amber might be. Considering the nature of the texts published in this paper, it has been often mentioned in the public that actually the name of Miroslav Miskovic is behind this Cypriot company, and, for a time, the name of Milka Forcan, his associate until recently. Control over this paper has also been ascribed even to Dragan Djilas, the mayor of Belgrade, the vice president of the Democratic Party (DS) and owner of the powerful marketing companies *Multikom Group* and *Direct Media*. Such doubts have been expressed by some parliamentary parties, but no one has ever managed to find out whose interests have been represented by the group of journalists since its establishment, when, in 2005, they separated from the then-editorial team of the tabloid paper *Kurir*.

It was exactly the appearance of the *Kurir* that contributed mostly to the tabloidization of the media and life in Serbia, and to the ultimate relativization of the problem of crime, corruption and, in general, the system of value. Certain political structures found the paper suitable because, on the basis of fabricated bombshells, it launched political knockouts; but then at a certain moment it turned against those who had supported it politically. All this made the political inspirators of *Kurir* drastically change the Law on Public Information and Broadcasting in 2009 in order to stop the paper they had themselves conceived, and then have arrested the owner of the *Kurir*, Radisav Rodic, who spent nearly two years in detention because of that. On 27 July of this year the High Court of Belgrade issued a verdict by which Rodic

was sentenced to two years of imprisonment, but he was immediately released, as he had spent the same period of time in detention. Otherwise, for years Rodic had just been playing a game with the domestic judiciary system, by establishing a series of related legal entities and off-shore companies that no one has ever managed to bring to court. After the arrest of its owner at the time, Radosav Rodic, the tabloid paper *Kurir* was taken over by his son Aleksandar Rodic, who is formally running the company.

Today Djoko Kesic, the present editor-in-chief of all the *Press* publications, Dragan Vucicevic, former editor-in-chief of *Press* and the present chairman of the Board of Directors of *Press Publishing Group*, and Svetomir Marjanovic, also one of the *Press* editors and a former journalist for *Kurir*, have six percent of the *Press* shares. A certain Biljana Kralj has 22 percent of the shares of this paper.

Since the absence of the true information about the media ownership,the conclusion about the owners are based on the editorial policy of the certain media, therefore, indicative is the attitude taken by the *Press* towards last year's Miskovic-Forcan affair, when this Miskovic's close associate left *Delta Holding*. Prior to that, the paper had never written critically about Miskovic, and that was the first time it published a negative perspective about him. In July 2010 *Press* ran such headlines as "Milka Return the Property", "Miskovic Sues Milka Forcan", but also "*Hamslade's* Claim Rejected in the Dispute with *Jugohemija*" and "*Jugohemija*: Promissory Note for *Deltastar*", and then the reporting was a bit "inconsistent". In *Novosti* the attitude towards the affair was clearer because this paper has not shown respect towards Forcan since the moment she left *Delta*, and the weekly *Vreme* was openly against Forcan. After the affair had calmed down, the *Press* wrote again positively about *Delta*, and also about Forcan's activities.

- **TV Prva and B92**

Though *TV Prva* and B92 are not the most popular television stations, their influence on public opinion in Serbia is enormous, particularly in the case of *B92* and its informative programme, while *TV Prva* is becoming increasingly more popular because of its entertaining programme. According to the applicable Broadcasting Law, the right to frequency use is the right to use a natural good, and thus media with national coverage are granted, together with the licence to broadcast a programme, also the right to use a public good belonging to all the citizens of Serbia. However, non-transparency of ownership often

enables the same owner to acquire this public good and a number of media with national coverage, which is contrary to the Law.

TV Prva, formerly *TV Fox*, is fully owned by foreign business, two Cypriot off-shore companies. The founder of *TV Prva*, the company *TV Fox*, is owned by the Cypriot company *Warraner Limited* (49 percent of the shares) and by the Belgrade company *Nova Broadcasting* (51 percent of the shares). The latter, a domestic company, is owned by another Cypriot off-shore company – *Antenna Stream T.V. Ltd*. Because of the off-shore structure of this medium, during the transfer process it could be found out only indirectly that the Greek shipowner Minos Kiryaku is behind these Cypriot companies. Speaking about the media, he confirmed that he had acquired *TV Fox* for one dollar from the American *Fox* owner, Rupert Murdoc. The Republic Broadcasting Agency (RBA) gave approval for this ownership structure, but it never disclosed publicly who the actual owner of the Cypriot companies is. In the graphic representation of the ownership of the TV station with national coverage, which was published recently on the RBA web site, it can be found that Minos Kiryaku controls 25 percent of the TV Prva through the off-shore company, and the 75 percent of this television are controlled by the three persons, whose surname is Kiryaku, and they are probably the members of his family.

TV Prva is an excellent example how ownership non-transparency, contrary to the Law, enables the same owner to acquire a number of media with national frequency. Specifically, in November 2010, *RTV B92* was sold. The domestic company *Astonko.*, owned by the namesake Cypriot company, became its majority shareholder, but its owner is unknown. However, information came from this medium itself that a certain Stephanos Papadopoulos is the actual owner of this Cypriot company, together with some other persons.

Papadopoulos is also the owner of TV Macedonia (http://www.maktv.gr/) from Thessaloniki in Greece, which is believed in this country to be a member of the Greek media group Antenna (www.antenna.gr/tv/), owned by Minos Kiryaku, which owns *TV Prva* in Serbia. According to the Register of Broadcasters in Greece, *Antenna* and *Macedonia* are formally unrelated TV companies, but actually *Antenna* has not only formally taken over the controlling package in *TV Macedonia* because of the Greek regulations on media concentration, but it controls this TV company. Therefore, there is a suspicion among the public that *RTV B92* and *TV Prva* have the same owner.

The Business Registers Agency (BRA) Council formally approved this ownership change, but it has never published the infor-

mation about the new, real owner of this media company; rather it has only stated that everything had been done in accordance with the law, though there are serious doubts of a violation of Article 99 of the Broadcasting Law resulting in forbidden media concentration. The RBA has recently published the graphic representation of the ownership structure of the radio and TV stations with national coverage, but it is still impossible to conclude who controls the TV B92. Stephanos Papadopoulos is named as a owner of the Cyprus off-shore company **Lake Blade Holdings,** which has 0,63 percent of the shares of the B92. This Cyprus company is the co-owner of the company Astonko, which has 84,55 percent of the B92 shares. The RBA does not publish data about the percent of shares which **Lake Blade Holdings** has in Astonko. The RBA only published that the ownership in the company Astonko have two Cyprus companies **Lake Blade Holdings** and **Salinik**.

- **TV Avala**

Zeljko Mitrovic, the owner of *TV Pink*, is mentioned to have also been the informal majority owner of *TV Avala* since March 2008, though formally he has only 4,95 percent share in it. It is assumed that through the Austrian company *Greenberg Invest*, whose real owners cannot be precisely established, and which owns 48.4 percent of this TV station, Mitrovic has the majority share in *TV Avala*, which would be also contrary to Article 99 of the Broadcasting Law and forbidden media concentration. The confirmation of this information was made in June 2011 when it was published in the media that Mitrovic was selling "his" *TV Avala* to *SMI Group*, which owned *TV Nova* in Croatia and after that the negotiation about the selling procedure started with the Al Jazeera.

Other *TV Avala* owners are businessman Danko Djunic, with 45.65 percent of the share, while the Institute of Economics, which is controlled by Djunic and Aleksandar Vlahovic, a DC MP and former minister of economy and privatization, has 0.99 percent of the share. Milosevic's former minister and deputy prime minister of the Federal Government, Djunic is considered to have been the creator of the privatization concept and one of the most powerful persons in Serbia. He is best known as the first man of the consulting company *Deloitte* in Serbia, which has been the privatization consultant in the sale of many domestic companies, but also as the co-owner of the mentioned Institute of Economics and the company *Eki Investment*. He has taken part in most of the disputable privatizations in Serbia, starting from Mi-

losevic's time, as an official in his government, until today, either as a consultant, or the owner of a company – from the first sale of *Telekom Serbia* to the Italians, until the liquidation of banks in Serbia, the sale of *Sartid* and *Imlek*, and numerous other domestic companies. His role was best manifested during the doubtful privatization of *C-Market*, when Miroslav Miskovic, Milan Beko and the former *C-Market* director, Slobodan Radulovic, made a cartel agreement, called the Memorandum of Understanding, at the premises of *Eki Investment*, following the initiative of the then-prime minister Vojislav Kostunica.

In comparison with other TV companies, *TV Avala* does not have a high viewer rating and influence on public opinion, but it is significant that this TV company represents the interests of an economic lobby. *TV Avala* mostly deals with topics which are suitable to its owners, and so, since 2008, it has had the exclusive right to broadcast auction sales by the Serbian Privatization Agency. Nevertheless, the greatest enigma regarding *TV Avala* is who is hiding behind the Austrian *Greenberg Invest*, whose formal owner had also owned, until recently, the domestic weekly paper *Standard*.

It should be reminded here that Zeljko Mitrovic has become the "Balkans media magnate", using the RTS infrastructure, owing to his close relations with the JUL party and the *Pink* cultural kitsch, while broadcasting his programme from one room in the building of the then-Central Committee in New Belgrade. At the end of the nineties, *RTS* was forced to give *Pink* all the required equipment against a small compensation, and owing precisely to the downfall of *RTS*, *Pink* started thriving. In the meantime, from this small JUL TV station, Mitrovic has built an empire, with TV branches in Bosnia & Herzegovina, Montenegro, Macedonia and Slovenia, with 15 specialized satellite channels (*Extra, Kids, Music, Plus, Movies*,...), musical and film production companies (*City Records, Pink Film International*), a marketing services company (*Media System*) and a CD factory (*Pink Digital System*).

Finally, it should be stated that it is worrying that even after the democratic changes in 2000, the issue of the downfall of *RTS* has not been opened, nor a claim made for compensation of damages caused to this RTV public service by the actions of *Pink*.

➢ Off-shore companies also in Radio Index and Radio Roadstar

Owners of radio stations also hide often behind off-shore companies, so that, out of a total of five national radio stations, as many as three have owners in Cyprus.

Radio Index has also a Cypriot owner – *SWF Investments Ltd.* from Limassol, which owns 49 percent of the shares. It is not known in this case either who the actual owner of these shares is, though some documents that can be found at the Business Registers Agency show that the director of the *SWF Investments Ltd.* from Cyprus is a certain Slovenian citizen called Leo Oblak. A person with this name is the director of the Slovenian group of radio stations, *Infonet Media*.

According to the data of the Business Registers Agency (BRA), the ownership structure of the *Radio Roadstar* shows that 49 percent of shares belong the Croatian company *Dijagram Nekretnine d.o.o. Zagreb*, whose core business is real-estate property trade. According to the BRA information, this change occurred in May 2011, and until then the 49 percent of shares had belonged to the Cypriot off-shore company *Radich Enterprise Limited*, while the remaining shares belonged to a certain Ilija Drazic, who is still today the owner of 49 percent of the shares. This is the third change in the ownership structure of this radio which was, according to the previous data, owned by *Euroluxpetrol-Elp* belonging to Borivoje Lazovic, who is still today registered with the BRA as the representative of this radio. According to media statements, this change in the capital of this radio happened after Lazovic's arrest in February 2009 under suspicion of committing the criminal act of association, receiving and giving bribes, and the abuse of office, whereby the budget of the Republic of Serbia was damaged by 25m dinars, but he was later cleared of all charges.

- **New Standard**

Until recently, 15 percent of the *Standard* weekly shares belonged to Zeljko Cvijanovic, while 85 percent of the shares belonged to the Vienna company *JK Zeitungsverlag Beteiligungs*. It is interesting that the owner of this company is the Austrian lawyer Werner Johannes Krauss, who is also the owner of *Greenberg Invest* in *TV Avala*. In the meantime the ownership structure of this magazine has changed so that 100% of the ownership was transferred to the company *NEW STANDARD MEDIA* belonging to Matilda Veljkovic, who was working at the marketing department of the old *Standard*, while the editor-in-chief was, and still is, Zeljko Cvijanovic. Cvijanovic is known to the domestic public as a journalist who was working during the war in the cabinet of the SDS leader Radovan Karadjic, and then he was the head of the SRNA Reporter's Bureau in Belgrade, a *Reporter* journalist, an editor of *Blic*

News, an editor of the weekly *Evropa*, whose alleged relations with the State Security Service have been reported on several occasions.

- **Ekonomist**

A very influential magazine where the attitudes of the economic elite can be read, *Ekonomist* operates in Serbia as the official publication of the company *Ekonom Ist Media Group*. The owners of this company are journalists Biljana Stepanovic Milosevic (10 percent) and Mijat Lakicevic (0.34 percent), but also the American company *Media International Group* (89.66 percent), which is operating within the American off-shore zone of the State of Delaware, and whose owner is unknown.

- **Objektiv**

The weekly *Objektiv* also has an owner in the same off-shore zone, the company *MGM Promarket*, whose actual owner can be only a matter of speculation. According to media statements, Boris Stajkovac, who is known to the wider public as the organizer of numerous humanitarian campaigns, the founder of the Children's Care Centre, but also a former high official of the Democratic Party and of Karic's Force of Serbia Movement (PSS). The fact that the deputy director of the company is Milica Stajkovac, his wife, supports the assumption that these statements are probably true. Stajkovac was otherwise arrested in March 2009 and then accused of a 2.7m dinar tax evasion.

- **Nedeljni Telegraf and Borba**

Nedeljni Telegraf (Weekly Telegraph), whose publishing ceased in 2010, also had a Cypriot owner, the company *Armapo Media Limited*. In spite of some speculations, it is not known who the owner of this company is either.

Borba, whose publishing also ceased at the end 2009, had a Cypriot owner too. The company *Buana Holdings Ltd.* from Nicosia is still the owner of the company *Novine Borba*, which used to publish the daily paper *Borba*. This Cypriot company bought the company *Novine Borba* from the company *Futura Plus* for 5,000 euros in October 2008. The *Futura Plus* is now owned by Stanko Subotic's companies *D-Trade* and *Emerging Market Investments* from Denmark, while the Cypriot

company *Buana Holdings Ltd*. was represented by the journalist Ivan Radovanovic, but its owner is not known.

Domestic politicians and businessmen as media owners

Besides the media whose owners originate from tax havens, there is a group of five media with insufficiently transparent domestic capital, which are actually owned by domestic businessmen or politicians – *TV Happy, TV Happy Kids, Radio S, Akter* and *Pecat*.

➢ **Happy**

The ownership structures of *TV Happy* and *TV Happy Kids*, two related TV companies sharing the national frequency, are concealed and complex. A certain Petar Ratkovic appears behind various companies as the ultimate owner of *TV Happy*, while a certain Dejan Nikolic is the owner of *TV Happy Kids*. Though there are no official reports, it is believed that *TV Happy* is owned by the controversial businessman Predrag Rankovic Peconi, because all the companies having a certain share in this TV station are registered in Zemun at the same address as the companies whose ownership in the media is attributed (though not officially) to Rankovic (*Monus, Invej*). Rankovic started business with gambling houses and betting offices, while the White Book of Organized Crime from 2002 shows him as the main money laundering operator of the "Surcin Clan". The Anti-Corruption Council has recently received a note from the employed journalists, expressing their suspicion that Zeljko Mitrovic is the informal co-owner of *TV Happy*.

➢ **Radio S**

Radio S is a radio station with a national frequency that is owned by a politician. *Radio S* used to be owned directly by the Socialist Party of Serbia (SPS), while it is now owned by Ljubinka Andjelkovic, mother of the high SPS official Zoran Andjelkovic, a member of the SPS Main Board and chairman of the MB of *Serbia Railways*. *Radio S* used to be owned by the company *Genes-S*, which was owned by SPS. Now it is formally owned by *AS Media*, whose founder is *S Media Team*, owned by Zoran Andjelkovic's mother Ljubinka.

➢ **TV Most and Palma Plus**

There are more evident examples in Serbia where party officials own media. *TV Most*, with a regional licence, is owned by Dusan Bajatovic, SPS vice president and director of the state-owned company *Srbijagas*; *TV Palma Plus*, which has regional TV frequency, is owned by Dalibor Markovic, son of the mayor of Jagodina and the president of the party *Jedinstvena Srbija*.

➢ **Pecat (Stamp)**

It is not possible to assert who the actual owner of *Pecat* is either, owing to the unusual cyclic ownership structure, which hides the actual owner. The company *Nas Pecat* publishes the paper, and its owner is the company *Baam-Trade* from Belgrade, which is owned by Branislav Vucelic (10.14 percent), Ana Vucelic (10.14 percent) and then again the company *Nas Pecat* (79.72 percent). However, Milorad Vucelic, who was a close associate of Slobodan Milosevic and an SPS official, is said by the public to be the actual owner of the *Pecat*.

➢ **Pravda**

The owners of the daily paper *Pravda* are also party members. They are Jugoslav Petkovic (47 percent), who is a member of the *Serbian Progressive Party* (SNS) and the chief of the municipal administration in Zemun, and Nemanja Stefanovic (48 percent) who is an SNS member, and it is related to Nebojsa Stefanovic, the vice chairman of the SNS Main Board.

➢ **Vojvodina Info Group**

Vojvodina Info Group, which has several regional print media is owned by party officials. Since its establishment in 2006 its ownership structure has changed, but, at the moment, it is the owner of the weekly *Zrenjanin*, *Somborske novine* (*Sombor News*), *Suboticke novine* (*Subotica News*), *Backopalanacke novine* (*Backa Palanka News*), *Vrsacke novine* (*Vrsac News*), while its share in *Gradjanski list* (*Citizens' Paper*) and the weekly *Akter* is unclear. The best known member of this media group is Dusan Stupar, former chief of the Belgrade Section of the State Security Service, and now one of the owners of the company *Universal Holding* and numerous domestic companies. Besides him, the other members of the Group are Srdjan Vucurevic, a *Democratic*

Party of Serbia (DSS) official of the Novi Sad City Council, and Nenad Romcevic, also a DSS official of the Novi Sad City Council.

➢ ***Radio Focus***

Another of the media whose owners are known by the public is *Radio Focus*, whose owner is the company *Interspeed*, owned by Petar Komljenovic from Belgrade. His name became known to the public during the police operation *Mreza* (*The Net*), undertaken against cigarette smuggling, and it was claimed that he was the leader of the group that worked under the patronage of Marko Milosevic. Bojana Kovacevic (Bajrusevic), who was also charged with cigarette smuggling in the nineties, and who is also known as the widow of Vlada Kovacevic, a.k.a. Tref, who was the actual owner of *Interspeed*, was also a witness before the Special Court in connection to his role in this. He was killed in 1997; that was the first in the series of killings of persons in Slobodan Milosevic's surroundings. He was close with Marko Milosevic and, according to the police information, the two of them were the cigarette smuggling bosses.

Quite a number of media experts have talked about the station's political bias toward the Serbian Radical Party (SRS) before the conflict in this party, and that it is now inclined toward the Serbian Progressive Party (SNS).

Journalists as media owners

➢ ***The weekly Vreme***

Among the national media there are only two owned by journalists themselves – the daily *Danas* and the weekly *Vreme*. However, the weekly *Vreme* did not manage to avoid the influence of big business to its editorial policy. Specifically, the owners of *Vreme* have a debt registered in the Loan Collateral Register because of a loan taken through the company *V Film* which has a registered debt of 370,000 euros to the company *Delta Maxi*[4], which will be due on 21 March 2012. In the meantime, the company *V Film* has been deleted from the Register, and it was affiliated to the company *Vreme*, which formally publishes the known weekly. The editorial policy of this weekly had changed in the meantime, which shows the significant influence of the *Delta* owner on the contents of this weekly's articles, especially regarding Miroslav Miskovic's business operation.

[4] under No. Zl.br.4149/08

This could be seen best on 3 March this year when *Vreme* published the "exclusive" information that Miskovic had sold the company *Delta Maxi* to the Belgian *Delhaize*, with a big photograph of Miskovic on the front page. In the affirmative text under the headline "World Trade in Serbia", Dragoljub Zarkovic, the editor-in-chief of *Vreme*, says that this transaction would "have probably been accomplished sooner if spokes had not been put into the wheels, which not only undercut the price of the regionally powerful retail trade chain, but this insinuation made a political issue of a serious trade transaction, where Boris Tadic, the president of Serbia, also once interfered". This is, however, only one out of a great number of texts in which Zarkovic defends Miskovic from the accumulated "allegations that would sometimes be funny even to deny" and which are for Miroslav Miskovic "probably the greatest threat as regards his position in the society"[5].

Foreign capital and the state as media owners

The daily papers *Blic, 24 Hours*, *Alo* and the weekly *NIN* are a part of the multinational German-Swiss publishing network *Ringier Axel Springer*. This group was created last year by the merger of the Swiss *Ringier* and the German *Axel Sringer*. A significant part of other Serbian media is still owned by the state. Besides *Politika*, *Novi Sad Dnevnik* and, partly, *Vecernje Novosti*, the state as the owner controls a great number of local media in spite of the fact that the Law on Public Information and Broadcasting provides for that the state cannot be a founder of a public media in Serbia, either directly or indirectly. These facts have only additionally contributed to the chaotic media situation in Serbia and it enables direct political control of the media.

Ownership abuse

The common feature of both the concealed media owners and the ones known to the public is the abuse of the frequencies for the purpose of achieving individual interests. Owners often treat the frequencies, leased to them as a public good, like their private property.

Perhaps the example of *Novosti* shows most illustratively the reasons and consequences of concealing the media ownership, which is done with the help of state institutions and reflects on the editorial policy of the media. Consequently, among other things, for years one has not been able to find in *Novosti* any analytical texts criticizing or prob-

[5] http://www.politika.rs/pogledi/Dragoljub-Zarkovic/t26551.lt.html

lematizing the business operation of Miroslav Miskovic or Milan Beko, nor of their companies and related persons. Even when they could not avoid denying certain unlawful actions, as in the case of the takeover of *Luka Beograd*, the editors of *Novosti* always managed to avoid it, publishing only texts with the message that "we shall all benefit from *Luka*" and that "everything was in accordance with the law", and it was always the same group of people sending the messages to the readers, including some officials, like Predrag Bubalo, but also representatives of the Securities Commission and the Serbian Privatization Agency.

Likewise, Miskovic and other big business owners are shown in this medium as "patriotic businessmen", "persons of trust", "successful domestic businessmen", "intelligent business persons", who are promoted through the headlines – "Businessmen Are Buying Plane Trees" (for the city), "Kraljevo (after the earthquake): Three Houses from *Delta*", "*Delta* Keeps its Word", "*Delta* is Conquering Slovenia Too", "Three Prime Ministers at *Delta*", "Dodik Wishes (to have) a Delta City", "Business Does Not Tailor Politics", "*Delta* Is Integrating the Balkans", "Businessmen are With the President", or "Serbs Behind *Salford*", "Anyhow, *Salford* Gets Ljubljana Dairy", "Beko: The Best are Leaving", etc.

Enemies are treated quite differently in *Novosti*, hence "Radulovic was Robbing Everyone", "Spanish Son-in-Law Launders Money", and there you could read headlines like: "Radulovic's Network for *Mercator*", etc. Especially impressive was the *Novosti* reporting when Milka Forcan decided to leave *Delta Holding*, when it was clearly seen who the boss was ("Milka Forcan Damages Miskovic"). How the owners' opponents are treated in *Novosti* is also shown in the text, entitled "Whom Does Barac Advise?", published on 9 February 2011, immediately after the announcement that the Anti-Corruption Council was working on a report about unlawful privatization of the media. This text is another example of drastic abuse of media because the aim was a showdown with the Anti-Corruption Council and its president, who publicly disclosed information about unlawful actions during the acquisition of *Luka Beograd*, because of which the Council has filed a criminal complaint against Milan Beko.

And not so long ago, *TV Pink* and *Novosti* reporting turned into a media war and showed how their owners, Zeljko Mitrovic and Milan Beko abuse media for achieving their individual interests. In February 2011, *Pink* suddenly started doing something this TV had **never** done before – investigative journalism. Over a few days this TV started "discovering" something about which certain media had been reporting long ago – that the sale of the *Novosti* shares had been carried out

unlawfully. According to the reports of other media whose attention was attracted by this conflict, the reason for *Pink's* sudden interest in the unlawful dealings with the *Novosti* was *Novosti*'s previous reporting about *Pink's* business fiasco in Slovenia, which then provoked this "counterattack" by *Pink*. In this "counterattack", in the middle of the February this year, beside the TV Pink, TV Avala took a part by transmitting almost the same news about the illegal privatization of the company Novosti. This fact showed the ownership connection between Pink and Avala.

When speaking about the abuse of media ownership, we should mention also the real private war fought for days by Zeljko Mitrovic against Croatia because of a dispute concerning his personal property, where he used the national frequency, which is a public good, for this purpose. The responsible Republic Broadcasting Agency (RBA) did not react to this example of drastic abuse of the national frequency in spite of calls by the journalist associations.

2. Financial influence of state institutions on media (buying influence) and the role of marketing agencies

The state institutions of Serbia spend significant budget money on advertising, which enables making personal and party promotions in the media. Annual spending by the state institutions on advertising in the media, based on a sample of the 50 most significant institutions from which the Anti-Corruption Council has obtained the data, exceeds 15m euros. When you add the funds which are officially assigned for the work of the media, we arrive at a figure of minimum 36m or even 40m euros paid to the media from state sources. If we compare this with the total market advertising, which according to some estimates amounts to approximately 160m euros, it means that the media get almost one quarter of their total income from state institutions. Thus the government gets a significant space for making its financial influence on the media, whereby it influences their editorial policy.

There is an actual need of state authorities for advertising regarding their different activities intended for the public, such as public procurement adverts, employment adverts, soliciting for tenders, etc. and such activities are precisely specified by the law. Article 86 of this Law provides that state agencies and organizations may advertise their activities and measures important for citizens, especially in five cases:

as messages calling them to participate in elections or a referendum, measures for citizens' actions in case of general emergency, humanitarian campaigns, public tenders and calls, as well as in the case of economic activities, such as buying off, purchasing, etc. The Law exclusively forbids the use of a name, image, voice or a similar feature of an official, or direct or indirect advertising of a political organization.

However, most of the funds paid to the media were given precisely through different types of campaigns that most frequently did not have a humanitarian character, as foreseen by the Advertising Law, but whose aim was to promote the work and activities of the relevant ministries. The most expensive campaigns so far have been "Let's Clean Serbia" by the Ministry of Environment and Spatial Planning, the promotion of the 'startup' loans by the Ministry of Economy, "Kosovo Is Serbia", the vaccination campaign against A H1N1 flu virus, the anti-smoking campaign, etc. For example, there is no advertising programme whose production was paid by the Ministry within the campaign "Let's Clean Serbia" where Minister Oliver Dulic does not appear as the protagonist.

Consequently, the publication of information on the work of state institutions has, over recent years, turned into banal publication of information on promotional activities of the officials who are in charge of state institutions, by the system "who pays more, gets more space". When, besides all this, the media get already-prepared and free video materials, as in the case of the two related companies – *TV Infobiro* and *Frame*, whose services of monitoring and recording of the events are paid by the ministries and other state institutions, and not by the media, then they do not have to send their teams to the field at all. *Infobiro* provides them all they ***need*** and what is ***desirable*** to be published. Therefore, among other things, the TV and radio contributions, such as texts in newspapers, are most frequently deprived of any research or analysis.

It should be also noted that the Law on Public Information and Broadcasting, Article 2, Paragraph 3, specifies that no one may even indirectly limit the freedom of public information, and especially not by the abuse of government or individual authorizations. Nevertheless, many budgets of state institutions are used exactly for the promotion of officials, ministers, directors and thereby their parties. According to the documents obtained by the Anti-Corruption Council, the company *Telekom Serbia* pays the biggest amount of money to the media

– the company for which it can be assumed that it has to advertise its mobile telephony services. However, this company is immediately followed by Ministry of Environment and Spatial Planning, then the Serbian Privatization Agency, then the Ministry of Economy and Regional Development, the Ministry of Health and the Ministry of Agriculture, the Institute of Health Batut, the Income Tax Department, the Electric Power Industry of Serbia (EPS), the Ministry of Interior, etc.

The examination of the Media Documentation Ebart[6] from 2009, which included the list of politicians who are the most often present in the media, partly matches the list of the state institutions who spend the most money on the media, or those that have budget-funded media relation agencies. The greatest number of newspaper articles and contributions have been dedicated to the work of politicians who paid the biggest amount of money to the media, and so Mladjan Dinkic, Ivica Dacic, Tomica Milosavljevic, Rasim Ljajic, Slobodan Milosavljevic, Nebojsa Bradic ... have appeared most frequently in them. In spite of the fact that the portfolios of the mentioned ministers are among the most attractive ones for the media and the public because of their importance, the fact is, the amount of the awarded media space for the activities of their ministries is not in concordance with the required quality of information, texts and contributions published by the media about the same. Specifically, the amount of funds spent on particular media does not decide only what space would be allocated for particular politicians, but rather these funds are decisive when certain events or the responsibility of government officials or civil servants should be relativized in the media.

Thus, for example, the news about the Council's Report on Unlawful Granting of Licences to the Company *Nuba Invest* for Laying Optical Cables was not even published by some media, and those which did published only scanty information about it. Unlike the Council's Report, Minister Dulic, whose ministry granted the licences unlawfully, was immediately given an opportunity by a greater number of media to present the positive results of the Ministry and to relativize the Council's Report. An illustrative example is how the media mitigated the unlawful actions at certain ministries established by the State Auditor Radoslav Sretenovic. The media showed special "understanding" towards precisely those ministries from the top of the list of those who spent significant budget funds on media activities.

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[6] http://www.danas.rs/danasrs/politika/dacic_i_dinkic_majstori_marketinga_.56.html?news_id=193096

Procurement through various models

The media have earned income from authorities and other state institutions in seven different ways, and the basic form was the publishing of advertisements, which has been ordered by nearly all state bodies. This basic form, which is foreseen by the Advertising Law, includes the lease of advertising space for publishing some concrete information important for the public, such as, for example, employment adverts, tenders for different projects, etc. Contrary to this basic form of advertising, the media also earned income on the basis of specialized information services, contracted information services, subscriptions to services, cultural subsidies, allocations of money from the funds foreseen for the civil sector for implementation of projects, and even for research services.

According to the Public Procurement Law, the regular public procurement procedure need not be carried out for research and development services, and a contract can be concluded directly; the same applies to the radio and TV programme production or programme broadcasting time. Thus, in 2009 the Agency for Small and Medium-Sized Enterprises ordered research services from the company *Ringier* (*Blic*), which included "research regarding the needs of small and medium-sized companies for the purpose of improving their business operation", with the obligation to publish the same in the daily paper *Blic*. The services were 4.48 m dinars worth, and their purpose was "the use of the research results by all of the public". Such jobs for which state institutions hire media, which are not professionally qualified for research such as this one, were used to hide the actual nature of the cooperation between the media and party officials who are in charge of state institutions, because the subject of such transactions is actually a free political promotion of party officials.

It should be emphasized here that the ministries and the state institutions that are responsible for such type of works, and which have qualified staff and which get the money from the budget, are supposed to do these works by themselves and should not engage anyone else for them. Thus in the concrete case, the Agency for the Development of Small and Medium-Sized Enterprises, which hired *Ringier* for said research, has been established to otherwise carry out research itself for the needs of small and medium-sized enterprises, as it gets budget funds for such purposes. It can also cooperate with other state scientific-research institutions that are already funded from the budget of Serbia, such as, for example, the Statistical Office of the Republic

of Serbia. However, it hired a medium, whose business is not essentially scientific-research work, to allegedly carry out the research; but, in fact, it is buying with that money advertising space and influence. Thus state politicians always get free promotion; the research required for the public is practically useless.

During this analysis the Council has discovered more similar examples where media were hired for research services, including the most drastic one in the cooperation between the Ministry of Environment and the newspaper *Blic*, whose obligation was to research and publish topical appendices about the environment for a compensation of 47.2m dinars.

Another significant model for hiding the actual nature of the relations between state institutions and "buying" influence in the media is subscription. Certain state institutions have paid subscription for news agency services, or access to "read" news and other agency reports, that are primarily intended for other media. Though most of these institutions already pay for press clipping services, the actual purpose of this cooperation is that the news agencies are "paid" to report on the work of particular officials, and consequently some institutions even concluded parallel contracts with several news agencies at the same time. In this way the institutions ensure better dissemination of positive and promotional news about the state authorities, as news published at a news agency service is more easily "transferred" to other media as well. In this way media lose some of the most important roles they have and the criteria they should meet, such as truthfulness and objectivity.

Over the last three years much more information and many more contributions have been published about institutions which paid such monthly compensation than about those which did not pay a subscription. The Ministry of Justice, the Ministry of Culture and the Ministry of Foreign Affairs have been subscribed to the news agency services. A mere search on the *Beta* Agency web site will show a total number of published contributions containing the term Snesana Malovic – 10,400, 5,560 with the term Nebojsa Bradic, and 562 contributions where Vuk Jeremic is mentioned. It is interesting that the name of President Boris Tadic appears only 1,510 times.

A number of media have been awarded the jobs to follow-up the activities of particular state institutions, which means that the journalists of those media acted as a service to these state institutions instead of informing the public objectively about the work of these institutions. This "follow-up of activities" boiled down to the actual promo-

tion of the work of the minister or director of a state-owned company or institution. The Advertising Law has been violated in a number of cases because the very official was promoted by the advertisement and not the information important for the public. Certain ministries and particularly public companies have indirectly practiced this. Thus, for example, the state-owned company *JP Srbijavode* leased space in the magazine *NIN* to publish promotional advertisements during 2008 and 2009, but actually these were interviews promoting the work of the director Nikola Marjanovic. When concluding business-technical cooperation, the media were also obliged to publish interviews with the minister or the director of the institution. Thus, within the contract for publishing the special appendix of the Ministry of Economy and Regional Development, *Blic* was obliged to publish interviews with Minister Mladjan Dinkic. According to the Law, such contents must be marked so that it can be clearly seen that it is a paid text, or a promotional advertisement, but this provision has rarely been observed by any medium, mostly because no politician finds it suitable that their "visionary" messages to the public be understood as paid promotional advertisements. On the other hand, the media do not find it suitable that such contents be clearly marked as paid, as in this way the true nature of their relations with the party and state officials and institutions would be disclosed.

A great number of such contracts between state authorities and media which were formulated as contracted information service, or specialized service, have been concluded below the nominal limit of the small-value public procurement, which enables that procurements can be carried out according to the less strict procedure. In 2009 this limit was 2.9m dinars. By an analysis of the contracts we have found out that at least 19 state institutions had contracts with agencies, concluded just below the big-value procurement limit exceeding 2.9m dinars (or 3.44m dinars including VAT). We have found forty or so such contracts.

➢ Telekom Serbia

Every year *Telekom Serbia* spends almost 30m euros[7] on marketing, but by this analysis we have found out that more than 10m euros is directly spent for media services. This is probably one of the rea-

[7] Telekom Serbia, "Report on Business Operation for 2009, Belgrade 2010, p.77 http://www.telekom.rs/Dokumenta/doc/telekom_godisnji_izvestaj_final_srpsk_%20za_internet%20prezentaciju.pdf

sons why it was almost impossible to find a text that would critically examine the problem of the sale of this company or an analysis of its business operation. The media mainly copy the official reports of the companies about their "successful business operation" and, therefore, the public is often deprived of the information about the indebtedness, economic reasons for the acquisition of the telecommunication companies in the Republic of Srpska and Montenegro, etc. Actually, during the privatization the public was regularly deprived by the media of a series of information that shed negative light on the "positive" topic of the privatization of *Telekom*. Thus the media did not publish the opinion of respectable and relevant experts who spoke negatively about the aspect of the privatization, but the sale was considered a "finished" matter by most major media, as well as by the ruling elite – so much "finished" that the media were more busy with the questions on what projects the money would be spent than with an analysis of the very sale. Some ministers were already "building roads" with money received from the sale, and all this so that the domestic public would accept this political platform, whose most probable interest was to have more money in the budget of the Republic of Serbia and consequently better chances to remain in power.

With an explanation that it is only advertising mobile telephone services, *Telekom Serbia* has contracts with most of the media in Serbia. The other two mobile telephone operators spend somewhat less money for marketing than *Telekom*. It spends most money for advertising on *RTS, RTV Pink* and *RTV B92*. In 2008 it spent 142.55m dinars for advertising on *RTS*, and in 2009, 124.02m dinars. In second place is *Pink*, which received from *Telekom* 92.82m dinars in 2008 and 136.05m in 2009. *TV B92* is in third place with 76.1m dinars in 2008 and 64.28m dinars in 2009. *Fox* is in fourth place on the TV list, while *TV Avala* is in fifth place. *Vecernje Novosti* had been the first among the print media by 2008, while *Blic* has taken over the leading position since 2009 (*Blic* made 43.25m dinars in 2008 and 58.95m dinars in 2009, while *Novosti* made 50.55m dinars in 2008 and 42.85 in 2009). Telekom paid significant amounts to other media as well, such as *Kurir* (47.40m dinars in 2008 and 35.40m dinars in 2009) and *Press* (34.57m dinars in 2008 and 40.92m dinars in 2009).

The data on the annual income share made by the media from *Telekom*, which ranges from 1.6 up to as much as 17.7 percent, show how important it is for the media in Serbia to have a sponsorship contract with *Telekom*. Thus, for example, *Telekom* spent 13.09m dinars for broadcasting commercials on *TV Avala* in 2009, while, according to

the Business Registers Agency, *TV Avala* made an operating income of 172m dinars in that year. It should be mentioned here that Aleksandra Radujko, the wife of the director of *Telekom*, Branko Radujko, was the editor-in-chief of this TV channel during that period. As to Branko Radujko himself, before assuming the office at *Telekom*, he had been the secretary general to President Boris Tadic.

The income of the daily paper *Danas* and *RTV B92* made from *Telekom* were about five percent in 2009. In October 2008 *Telekom* sponsored the broadcasting of the Champions League matches in 2008/09 (9.2m dinars) on *TV B92*, then in December of the same year it sponsored the programme *Operation Triumph* (29.2m dinars), and, in January 2009, the New Year's special feature, *Storks in the Fog* (*Rode u magli*), and at the end of that year it sponsored the series programme *Big Brother* (35.4m dinars including PDV).

- **Ministry of Environment and Spatial Planning**

Telekom is immediately followed by the Ministry of Environment and Spatial Planning, which spends more than 1.5m euros for promotion, though it need not advertise "its" products. A media sector should be justifiably added to this Ministry, considering the amount spent, which they do not show as advertising but as research or provision of specialized services. In 2009 this Ministry spent just over a half million dinars on advertising, but from other budget items it spent between 130 and 150m dinars on promotion, buying promotion space in the media. Minister Dulic concluded the most significant contracts with *Ringier* (*Blic* and *Alo*) for environment research services, amounting annually to nearly half a million euros (47.2m dinars). *Ringier* undertook the obligation to publish the research results in the daily papers *Blic* and *Alo*, so that the research results would be accessible to the public. Even though on the Blic web site a lot of articles about this area could be found, there is no texts on the research conducted by *Ringier* could be found by searching the *Blic* web site, with an indication that they have been paid by the Ministry, though there are many contributions dealing with the area. On the other hand, during 2010 alone *Blic* published a lot of texts in which Minister Oliver Dulic is mentioned, most frequently in a positive context: "Dulic Is Taking 200 Builders to Kraljevo", "Environment Better Than in Previous Year", "1633 Apartments Will Be Built Next Year", "Politicians Fell for Facebook", etc. We could find only rare critical texts related to the proceeding initiated against him by the Anti-Corruption Council because of allegations of

possible conflict of interest, due to the fact that his company *DG Comp* was doing business with 70 companies and institutions financed from the budget of the Republic of Serbia. The consequence of the cooperation between media and state institutions can be relativization of the actions of the state officials and media are used to mitigate the public reaction, instead of being protagonists in discovering unlawful actions and corruption of state authorities.

- **Serbian Privatization Agency**

The Serbian Privatization Agency is in third place with an annual spending of about 62m dinars and probably because of that a great majority of the media start informing the public about the privatization problems only when some privatization is officially revoked. The Agency spends most of the funds on print media – *Vecernje Novosti, Blic, Politika* and *Press*. It is interesting that the services of the TV broadcasting of auctions are provided by *TV Avala*, owned by Danko Djunic, who otherwise provides a greater number of consulting services for the Agency. According to the contract for TV broadcasting of auctions, signed in February 2008, *TV Avala* gets 850 euros for broadcasting an auction and 350 euros for the broadcasting costs and 500 euros for the production costs. However, the contract does not define the time schedule or the number of auctions broadcast on an annual level and, therefore, it is not possible to calculate how much money *TV Avala* has made for this service.

- **Ministry of Economy and Regional Development**

The Ministry of Economy and Regional Development follows the Agency with annual spending exceeding 60m dinars, which can be also a reason why there are almost no critical reports about it in the media.

Most of the funds have been paid for the services of TV channels with national frequencies: *RTV B92, RTS* and *RTV Pink*. The claims of the now already former minister Dinkic that he could not promote his work are not true considering the budget spending for media because this Ministry has had all the national TV channels on its payroll. Even a number of media started a campaign defending the former minister after his removal from the office. Those days Dinkic was on the front page of the *B92* web site a number of times, and his activities were regularly followed up in the informative programme of this TV chan-

nel, though he was then only the leader of the parliamentary caucus the United Regions of Serbia.

TV B92 has made 14.34m dinars, *Pink* 14.18m dinars and *RTS* 11.06m dinars from the Ministry of Economy and Regional Development. The print media received 2.7m dinars from this Ministry in 2009. In 2009 *Novosti* followed up the work of the Ministry in their Internet edition www.novosti.rs for a compensation of 210,000 dinars and it prepared the map of the Spas of Serbia for 290,000 dinars. In 2010 *Blic* prepared and published a special appendix in the area of economy for an amount of 590,000 dinars, where publishing of interviews with Dinkic was specially foreseen. In 2010 the magazine *Status* got a job from the Ministry to follow up the work of this institution for 3.3m dinars, with the obligation to publish a text about its work in each edition.

- **Ministry of Health**

The Ministry of Health spends about 35m dinars on promotion in the media. Most of the money was spent on the vaccination campaign against the H1N1 virus "Roll Up Your Sleeve" ("Zavrni rukav"). That is the reason why a small number of the media reported objectively about the transaction of the urgent purchase of the vaccine against the H1N1 virus in 2009 and, therefore, instead of having objective information, the citizens received from the media only calls to get vaccinated. The responsibility of the Ministry of Health and Minister Tomica Milosavljevic in this transaction was rarely questioned in the media, though it turned out eventually that the purchase was disputable and the quantity of the purchased vaccines excessive and unnecessary.

The newspaper *Politika* rarely objectively reported on this problem, but during that period it made 3.22m dinars from this Ministry, second to *TV B92* which made 5.53m dinars for broadcasting related commercials. In 2009 the Ministry spent direct budget funds also on the *Blic*-promoted project "The Human Body Atlas", amounting to 2.36m dinars, but it was not shown as advertising. The Health Institute Batut is also related to this Ministry, with an annual spending of about 34m dinars for promotions, which have been mainly anti-smoking and some other anti-addiction campaigns; therefore, it is not unusual that reports on Batut are mainly positive. In 2008 *RTS* received 5.8m dinars from Batut, *B92* 4.97m dinars, *TV Avala* 2.74m dinars and the daily paper *Danas* 1.2m dinars.

➢ **Ministry of Agriculture**

In 2009 the Ministry of Agriculture spent more than 30m dinars on promotions, but the money was spent through several marketing agencies and, therefore, it cannot be found out which media published the promotional adverts. At the same time there is an impression that the situation in this area has deteriorated over the past period, while the media popularized the activities of the Ministry instead of writing about topics important for agriculturalists. Thus the ecological appendix of *Politika*, "The Green Pages", published in 2008, was also obliged "to support in the texts the activities of the Ministry" because of the paid 2.4m dinars. For the topical appendix "*Blic* Agriculture", published in 2010, the Ministry was to pay *Blic* 510,000 dinars per appendix (total 5.12m dinars), and in accordance with it Minister Dragin appeared more frequently in *Blic*, as well as on *TV B92* because in June 2010 the Ministry paid 3m dinars for ten programmes of "Magnification" ("Uvecanje").

➢ **Ministry of Work and Social Policy**

In 2008 the Ministry of Work and Social Policy spent 28.3m dinars on media and promotion and 15.56m dinars in 2009, but most of the funds were spent through the agency *Maxim Media* and, therefore, it cannot be found out which media received the money.

➢ **Ministry for Kosovo and Metohija**

The Ministry for Kosovo and Metohija spent the most money on advertising in the media in 2008 at the time when Slobodan Samardzic was the minister, i.e. 21.42m dinars, while a much smaller amount was spent in 2009.

➢ **Ministry of Interior**

The Ministry of Interior spent 14m dinars keeping the public informed in 2008, 8.89m dinars in 2009, but the report we have received does not specify the names of the media. The Ministry of Interior advertised itself in *Blic* in the encyclopedia project "All About Serbia" ("Sve o Srbiji") (590,000 dinars) but it is not stated when exactly. The flyer-inserting project on visa liberation was also carried out (680,000 dinars), but there is no the data on what media were involved.

- **Tax Administration Department**

The Tax Administration Department has advertised itself mostly in printed media (21.62m dinars in 2008 and 23.48m dinars in 2009) and has spent most on the newspaper *Danas* (3.4m dinars in 2008 and 6.4m dinars in 2009).

- **National Employment Office**

The National Employment Office (NSZ) spends 17m dinars annually on promotion in media, mainly in electronic media, and thus it spent 980,000 dinars on advertisements in printed media. In the same year it spent about 11.85m dinars for production of programmes on *TV B92*, and in 2010 it spent about 3.9m dinars. In May 2009 the NSZ paid 1.95m dinars to the newspaper *Danas* for the insertion of the publication "Poslovi" ("Jobs").

- **State-owned company Electrical Power Industry of Serbia (EPS)**

From 2008 to 2010 the state-owned company Electrical Power Industry of Serbia (EPS) paid 14.63m dinars for media services and cooperated with *TV Happy* on the promotion campaign "EPS and Children" ("EPS i deca"), which cost nearly 1m dinars. EPS paid the largest amount to the daily paper *Danas* – 2.6m dinars, but EPS spent 2.4m dinars on advertising in *Politika*, and 1.26m dinars in *Vecernje Novosti*. A public polemic on the need for advertising this monopolistic electrical power supply company was opened, especially in September 2010 when it was disclosed that this state-owned company, which was one of the companies with the biggest deficit, was to pay 800,000 euros to the football club Partizan, sponsoring it in the Championship League and other international matches until the end of 2011.

Influence of agencies for relations with media and private production companies

Public relations agencies, marketing and production companies, which are mainly owned by party activists or persons related to them, have a special place in the relations between state institutions and media. Some of these agencies provide services to most of the state institutions, so that some of the agencies receive income exclusively from state bodies. A number of state institutions and state-owned compa-

nies have specially hired agencies for relations with the media or production agencies, in spite of the fact that they have entire services of their own whose job is to maintain relations with media. Therefore, engaging companies for such jobs is not only disputable, but it is also problematic because its purpose is mainly the political promotion of the work of ministers and directors, and not informing the public.

Out of the 22 ministries of the Government of Serbia covered by the Council's analysis, only three ministries have not used the services of these agencies (Ministry of Science, Ministry of Education and Ministry for Public Administration and Local Self-Government). Among the ministries, some hold a record in the use of services of the biggest number of agencies, such as the Ministry for Kosovo and Methoija, which used the services of eight different agencies in 2008. Over the last three years, as many as 11 agencies worked for the Ministry of Agriculture, and some agencies were also hired for particular departments within this institution. The Ministry of Health has hired 10 agencies, and seven agencies worked for it in 2009 alone.

Moreover, these agencies, whose owners are most frequently high party officials or persons related to them, have controlled the advertising market for years. These agencies, actually, lease advertising space from media, and then they sell it to their clients or individual buyers at much higher prices. While working on this Report, the Council met with representatives of the company *McCann Ericsson*, who explained that they get these jobs because the media, which are in a poor financial situation, agree, under the condition of advance payment, to lease advertising space at lower rates than the actual market rates. However, according to the information obtained by the Council while researching this phenomenon, it happens that these agencies pay the media only a part of the contracted advance payment amount, and the payment of the remaining part is used to exert pressure on the media, and they stop paying if the medium starts pursuing a topic which is not in the interest of the agency owner's party, or if it is not in his personal interest.

Distribution of agencies by political parties

The analyzed contracts clearly show the party distribution of agencies, so that, for example, the agency *A Media* provides services to institutions controlled by G17 Plus activists, such as the state-owned Public Water-Management Company (*JVP Srbijavode*), or the National Agency for Regional Development, the Republic Institute for Sport,

the Republic Institute for Health Insurance or the Grammar School of Kragujevac. That should not come as a surprise, as the director of this agency is Tomislav Damnjanovic, former chairman of the G17 Plus Executive Board and the creator of its campaigns. Damnjanovic is also the brother of Mladjan Dinkic's wife Tatjana. The Association of Independent Electronic Media (ANEM) has the biggest ownership share in this company (40 percent), then Mitko Jakovleski (10 percent), and then Veran Matic (*RTV B92* editor-in-chief), Sibina Golubovic, Tomislav Damnjanovic, Tatjanja Boskic (five percent), etc.

The Ministry of Health, at the time when Tomica Milosavljevic was the minister, also was in active cooperation with the agency *Cross Communications*, owned by Svetlana Blagojevic, who organized the campaigns called "Serbia Against Cancer". In order to promote a campaign against cancer, in 2009 this Ministry paid for the production of the TV series "The Village is Burning and Granny is Combing Her Hair" ("Selo gori a baba se ceslja") (8.35m dinars) through the consortium *Contrast Studios* and *Media House*. Blagojevic's agency also worked on the campaign "Click Safely" ("Klikni bezbedno"), which was given 2.5m dinars by the Ministry of Telecommunications, controlled by G17 Plus officials.

The agencies *McCann Erickson Group* and *Stoa* provide services to state-owned companies and state institutions controlled by DC officials, such as *Telekom Serbia*, the Ministry of Agriculture, the Ministry of Trade and Services or the Ministry of Foreign Affairs. The agency *Stoa* has already been working for the Assembly of the City of Belgrade for several years, as well as for the Assembly of the City of Novi Sad, which has been traditionally controlled by DS.

The agency *Profiler Team*, owned by Goran Veselinovic, where, according to the SRS information, SNS deputy president Aleksandar Vucic is employed, was providing PR services to the Ministry of Mining and Energy for a monthly compensation of 300,000 dinars, but since SNS has taken over power in Zemun and Vozdovac, this agency has received between 300 and 400 thousand dinars every month. It is interesting that the *Profiler Team* does not have any other clients among state institutions, except only where SNS is in power.

Before losing power, DSS and Nova Srbija had also had their favourite agencies, which can be seen best in the example of the agency *Arts & Crafts*, owned by Miljan Scekic, which did a number of jobs for the Ministry for Kosovo and Methohija in 2008, for a total amount of 7.87m dinars. The agency printed table calendars, put up posters,

billboards and produced TV programmes, and all that within the campaign "Kosovo is Serbia". They created billboards with dominating photos of world leaders and their statements regarding the preservation of the country and democracy. In that year the agency made an income of more than 20m dinars, but the next year it made only 1.32m dinars; therefore, it can be concluded that it was surviving owing to the jobs obtained by political support, primarily by DSS and NS. Scekic was advisor to Maja Gorjkovic at the time when she held the office of the mayor of Novi Sad, and his agency also organized the Nova Srbija presidential candidate campaign of Velimir Ilic in the elections of 2008. A series of other agencies (*Grifon Media, Masel Group, Mediana Adria*) and two related companies for the production of documentary films about Kosovo – *Ronin Pro* and *Sans Oil* – which are now in liquidation, were also hired within the frame of campaign "Kosovo is Serbia".

- *Personal predisposition towards certain agencies*

The analysis of the documentation shows that certain agencies provide services to a series of institutions related to the work of a particular politician. Thus the agency *Stoa*, although deprived of other bigger jobs, has always been engaged where Minister Sasa Dragin was. When he was the Minister of Environment from 2007 to 2008, *Stoa* was doing PR for the Environment Protection Fund, and when he took over the Ministry of Agriculture, the agency *Stoa* became the most favourable agency for this Ministry, but it was particularly hired by some bodies which are a part of this institution (General Inspectorate of the Ministry and the Department for Agricultural Payments). The Ministry of Agriculture separately paid the agency *Stoa* for information services (3.39m dinars), and separately for the services informing about the General Inspectorate of the Ministry of Agriculture and the Department for Agricultural Payments. The owner of the agency *Stoa* is Ljubomir Podunavac, a political scientist and a DS activist, who is presently, besides working for his agency, also the director of the *RTV Sabac*, with which this Ministry also has business cooperation, while the wife of this marketing expert, Jelena Kosanic Podunavac, has been since recently the head of the *RTV B92*.

Furthermore, the Ministry of Agriculture also had contracts with a greater number of other marketing agencies: *McCann Erickson Group, Media S SMVG, Ebart, Can Advertising, Grafoprojekt, Ideological Factory, Infobiro, Milk & Honey Communications* and *BimBros*. In 2008 *Grafoproject* produced four TV programmes entitled "Agroworld"

("Agrosvet") costing 2.2m dinars, which were to be broadcast on 53 local TV stations, and the next year the same programmes were produced by the related company *BimBors*, belonging to a certain Zoran Vasiljevic, for a compensation of 3.06m dinars.

Among the agencies hired by the Ministry of Agriculture there is a certain number from Novi Sad, such as the *Ideological Factory*, which was hired in 2009 for shooting an educational informative spot for the Ministry, costing 3.33m dinars, which was the only income of this company in that year. The owner of this company is a certain Vujadin Vukmirovic, and the director Pedja Popic, both from Novi Sad and members of the *Rotaract Association*, the so-called *Rotary Club*, where Minister Dragin was active as well. At the same time Dragin hired another Novi Sad company *Milk & Honey Communications* to buy media time for an amount of 12.03m dinars. The owner of this company is a certain Goran Ivetic, who was on the MP candidates list for the Force of Serbia Movement.

The Minister of Agriculture, Slobodan Milosavljevic, in the period from 2007 to 2008 engaged the agency *Communis* for PR services; the same agency was "transferred" together with him to the Ministry of Trade and Services and was the most favourable there. The *Communis* is owned by Ivan Stankovic, who is known by the public as one of the first domestic marketing experts, the founder of the first marketing agency in Serbia, *Saatchi&Saatchi*. *Communis* created communication projects "We Give" ("Mi dajemo") for the Ministry of Agriculture for compensation of 15,000 euros and the production of 26 TV programmes called "Agro Prognoses" for an amount of 26,000 euros. We found another contract for the same programmes, which was later on cancelled; but it was with another agency – *Media S SMVG*, whose owner is also Stankovic. Besides these contracts, in 2008 the agency provided specialized information to the Ministry of Culture for an amount of 2.68m dinars and radio spots for the Ministry of Trade and Services (2.6m dinars), promoting the development of trade in Serbia. The Belgrade Airport also engaged the *Communis* in 2008 for marketing presentation and production of films, and the value of the contract was 93,915 euros.

- **Multikom Group, Direct Media, Emotion**

Agencies in which Dragan Djilas, the mayor of Belgrade and Democratic Party deputy president, owns a share have a significant place on the marketing and advertising market. Djilas owns one quar-

ter share in the marketing agency *Multikom Group*, in which he used to have a half share, while now the other quarter is owned by Milica Delevic, the director of the European Integration Office of the Government of the Republic of Serbia. The company *Multikom Group* was established in 2004, and its business is related to advertising in media, leasing media space, financing productions, purchase and sale of TV rights, etc. *Multikom* has shares in other agencies, i.e. 93 percent in *Direct Media*, whose business is also sale of advertising space. Three companies called *Direct Media*, operating in Macedonia, Bosnia and Montenegro, with seats in Skopje, Sarajevo and Podgorica, are members of this Group.

Multikom Group is the majority owner of the domestic companies *Spark Event Promotion*, a company for promotional activities, *Sports ADD* accounting services, *Big Print* for printing services and *Frendee* for Internet trade, while the production company *Emotion*, in which *Multikom* had been a co-owner with a 49-percent share, produces the most expensive TV programmes, such as "Big Brother", "48-Hour Wedding Party", "All for Love", "Swapping Wives", "Operation Triumph", "Take It or Leave It", etc. According to the data obtained by the Council from the Business Registers Agency (BRA), *Multikom* was deleted from the Register as co-owner in the production company *Emotion*, and *IMGS*, owned by Goran Stamenkovic, has been registered as its sole owner, which had had a 51-percent share until this change in the ownership structure of *Emotion*.

According to the BRA data, *Multikom* and *Direct Media* have had a constant growth of net profit from year to year. In 2008 *Direct Media* made a net profit of 558,628,000 dinars, while in the previous 2007 its profit was lower by almost 200m, amounting to 380,604,000. In 2009 its net profit was 619,679,000 dinars, and in 2010 it was 758,994,000 dinars.

It was similar with *Multikom Group*, which, together with related companies, made a net profit of 498,432,000 dinars in 2008 and 563,130,000 dinars in 2009, while in 2010 the net profit amounted to 790,216,000 dinars.

According to the data obtained from the NBS Treasury, the Anti-Corruption Council learned that the printing house *Big Print*, which is a member of *Multikom Group*, also has direct business cooperation with state institutions, including those funded from the budget of the city of Belgrade, whose mayor is Dragan Djilas. This company provides services to the Assembly of the City of Belgrade, the city municipal-

ity of New Belgrade, to most Belgrade theaters (*Atelje 212, Zvezdara Theater, Belgrade Drama Theater, Yugoslav Drama Theater*, etc.), and also to the Tourist Organization of the City of Belgrade, the Belgrade Library, the Cultural Centre of the City of Belgrade, the Youth Home, and the Health Centre of Rakovica. *Big Print* has also provided services to the Historical Museum, the Pedagogical Museum, the National Museum, the Museum of the History of Yugoslavia, and the Serbian Academy of Science and Arts.

According to press statements (http://www.standard.rs/vesti/36-politika/6687-slobodan-antoni-mrea-kolskih-drugaraq-u-politikoj-eliti-srbije-.html), Dragan Djilas, through his agencies, controls the leasing of the biggest part of the advertising space on national and regional televisions in Serbia. In order to check this information, on 27 September 2010 the Anti-Corruption Council submitted an application to *RTS* to access information of public importance, requesting contracts for advertising in the media concluded with marketing agencies from 2007 to 2010. As *RTS* has not furnished most of the requested documentation to the Council, we could not examine this problem. We shall present the conclusions we have made on the basis of the requested documentation *RTS* has furnished, in the part of the Report dealing with the role of this public service.

- **McCann Erickson**

During the last three years the *McCann Erickson Group* agencies have worked for seven ministries (the Ministry of Agriculture, the Ministry of Foreign Affairs, the Ministry of Economy and Regional Development, the Ministry for National Investment Plan, the Ministry of Health, the Ministry of Mining and Energy and the Ministry for Work and Social Policy), and on the basis of the answers we got from the state institutions we have found out that the Republic Telecommunications Agency, the Construction Directorate of Serbia and the Medicines and Medical Devices Agency of Serbia (ALIMS) have also been clients of this Group. However, according to the Treasury Directorate, from 2007 to 2011 the *McCann Erickson Group* agencies have provided marketing services to a total of 103 budget beneficiaries, or state institutions. There have been the highest state bodies among them, such as the President of the Republic of Serbia, the Government and ministries of the Republic of Serbia, and a great number of state-owned companies, such as the state-owned company *Roads of Serbia* (*Putevi Srbije*), cultural institutions, such as the *Terazije Theater* or the

Cultural Centre of Novi Sad, state institutes and agencies, such as the Serbian Privatization Agency or the Health Insurance Institute, local self-governments, such as the self-governments of the City of Belgrade and of the municipalities of Novi Beograd, Vracar and Zvezdara, or of the Municipality of Paracin, clinical centres, such as the Clinical Hospital Centre of Bezanijska Kosa, health centres in Lazarevac and Leskovac, schools and faculties, and even judiciary institutions, such as the High Magistrates Court of Belgrade.

The vaccination campaign of the Ministry of Health against the flu virus A H1N1, costing 6.7m dinars, was the best known campaign of this marketing agency. However, the most significant marketing services of *Universal McCann* (since recently *Universal Media*), a member of *McCann Erickson Group*, have been provided for *Telekom Serbia*, which has a group of hired agencies, for production and media relations.

This agency is owned by Srdjan Saper, member of the DS Presidency and an informal advisor to the President of Serbia, Boris Tadic, who organized various pre-election campaigns. The magazine Status wrote about this Saper's informal role in June this year, as well as President Tadic himself. In a conversation with Svetislav Basara, Tadic said:

"It may sound very apathetic how I got involved in this. And I got involved in all this when four of us, my childhood friends and I met one night and talked about whether Serbia should be *given up to the Radicals... There were only four of us...

Basara: You, Krle, Saper, and who was the fourth?

Tadic: Tucko. The four of us."

Following the proposal of the Government of Serbia, Saper also became the chairman of the Management Board of the Belgrade Philharmonic Orchestra, with which, according to the statements of the Treasury Department, his agencies have direct business cooperation, which constitutes a conflict of interest.

The agency Universal Media operates within the big marketing network *McCann Erickson* for SE Europe, which operates in Serbia, Montenegro, Macedonia and Albania, whose head is also Saper. This marketing network represents some of the biggest domestic and foreign companies and makes decisions about the biggest marketing budgets in the region. Its annual turnover is, according to the statements of the company itself, about 25m euros in the region and, according to the BRA data, in Serbia alone, *the companies belonging to this Group (McCann Group, McCann Erickson, McCann Erickson Public Relations*

and McCann Erickson Clipping) made an income of about 1.19 billion dinars, which is about 12 million euros.

The agency *McCann Erickson Public Relations* had receivables from the budget institutions in amount of almost 26m dinars only in 2009, which shows a significant increase in comparison with 9.8m dinars, which it received from these institutions in 2007. According to the BRA data, *McCann Erickson*, a company for marketing and market communications, which is 100-percent owned by Srdjan Saper, owns 40 percent of the shares of the *McCann Erickson Public Relations*, while Borislav Miljanovic, a former *BK TV* journalist, owns 60 percent of its shares.

At the same time during 2009, the agency *McCann Erickson Press Clipping* (now *Real Time Clipping*), which was established at the end of 2008, had an increase of its income from the budget institutions, as some of the jobs and the budget institutions were "channelled" into it. This agency has had a total annual income from state institutions amounting to 7.1m dinars in 2009, and 6.5m dinars in 2010. It should be mentioned that the net profit of this agency has constantly grown since its establishment in 2008. Thus, in the first year of its operation – and it is important to say that *McCann Erickson Press Clipping* was established in October 2008, which means soon upon the formation of the present Government of the Republic of Serbia and the assumption of the power by the Democratic Party – its net profit was 35,000 dinars, the next year, 2009, it was 7,866,000, and in 2010 it reached an amount of 8,856,000 dinars.

McCann Erickson Press Clipping (or *Real Time Clipping*) is now owned 100 percent by said Borislav Miljanovic, as, according to the information from *McCann Erickson Group*, Srdjan Saper sold his 51-percent share after the "Philharmony Affair". It is worth mentioning that it was learned that, at the beginning of this year, this agency concluded business contracts with the Belgrade Philharmonic Orchestra, where Saper is the chairman of the Management Board, which puts him in conflict of interest.

It is also interesting that the amounts paid for services to the *McCann Erickson* agencies mainly did not exceed the legal minimum for conducting the regular public procurement procedure, or they were within the limit of the small-value procurements, which is otherwise characterized, in analyses of corruption in public procurement, as the area where the largest budget funds are spent without any control.

Besides the marketing services provided to *Telekom Serbia* by *Universal Media*, a member of *McCann Erickson Group*, this compa-

ny has signed many contracts with the production company *Adrenaline*, which is also a part of Saper's Group and 100-percent owned by him. In 2008 *Telekom* sponsored *Adrenaline* with 23.28m dinars for 30 episodes of "Karaoke Showdown" ("Karaoke obracun") on *TV Pink*; then 4.68m dinars was paid for 20 episodes of the programme "Genius Show" ("Genijalni sou") on *TV Avala*; in 2009 it paid 28m dinars for the series "I've Got Talent" ("Imam talenat"); and then, last year, it paid 26.6m dinars for the series "The Sixth Sense" ("Sesto culo").

➢ Initiative, Media Pool

In 2008 and 2009 Telekom Serbia obtained marketing services also from the agency Initiative, owned by *Lowe & Friends*, whose only owner now is one of its founders, Branimir Dimitrijevic Tucko. Specifically, in 1990 he established *Lowe & Friends* together with Saper and Nebojsa Krstic, official adviser to President Tadic and the owner of the agency *Nova Communications*.

Media Pool is also one of the agencies which cooperated with *Telekom* in 2010. According to the Contract for promotion of this company in the TV series "The Village is Burning and Granny is Combing Her Hair" ("Selo gori, a baba se ceslja"), *Telekom* was to pay 28.71m dinars. *Media Pool* is owned by *Magna Europe*, a company from Macedonia, but in contracts with *Telekom* Tatjana Pantic, who had previously represented Saper's *Adrenaline*, appears as the director of this agency.

➢ Morfeus Group and Morfeus Direct Communications

The name of Tatjana Pantic appears also with the *Morfeus Group*, which has concluded with the Ministry of Environment and Spatial Planning deals worth dozens of millions of dinars. Until 16 August this year Tatjana Pantic had been registered as the owner of 34 percent of the *Morfeus Group* shares, while 66 percent belonged to Maja Totovic, who was, according to the data from her personal CV, the director for strategic planning at *McCann Erickson* from July 1998 till February 2007.[8] As of the mentioned date, Maja Totovic has been registered as the 100-percent owner of *Morfeus Group*. It is indicative that this change in the ownership structure happened after the aforementioned meeting which the members of the Anti-Corruption Council had with representatives of *McCann Group* while working on this Report. Specifically, at this meeting, which was held on 2 August this year, the Council members were told that no indirect conclusion regarding any

[8] http://www.linkedin.com/pub/maja-totovic/26/10a/147

relation between *Morfeus Group* and *McCann Erickson* should be made "only on the basis of the fact that Tatjana Pantic had been a former director of *Adrenaline*". The representatives of this agency added that Maja Totovic used to work for *McCann Erickson*, but that she had never been a director of this agency. While writing the conclusive parts of this Report, we noted that in the meantime, or within a period of only two weeks upon the meeting of the Council's and *McCann Erickson*'s representatives, the ownership structure of *Morfeus Group* was changed and the name of Tatjana Pantic, who had doubtlessly been the director of Saper's *Adrenaline*, was deleted from the Register.

In December 2008 Maja Totovic established the company *Morfeus Direct Communication*, which already in the first year of its operation, 2009, and with only three employees, made a net profit of 6,452,000 dinars.

In 2009 the *Morfeus Group* had the most valuable marketing contract among the agencies, concluded with the Ministry of Environment and Spatial Planning, worth 47.2m dinars, for production of spots and purchase of media time within the campaign "Let's Clean Serbia" ("Ocistimo Srbiju").

No financial report on the campaign "Let's Clean Serbia" has ever been published, but with regard to the documentation it can be said that in 2009 the Ministry spent 100m dinars on this campaign, and in 2010 not less than 120m dinars. This has been the biggest expenditure of a state body on a media campaign in recent times. Besides the fact that the results of this campaign can hardly be measured exactly, the promotion of the personality of Oliver Dulic, minister and a DS official, is also disputable. This can be seen specifically on the web site www.ocistimosrbiju.rs (about whose disputable creation the public of Serbia has already been informed), where the programmes and advertisements, created within the production of this campaign, can be seen in the Gallery section. Minister Dulic appears in a significant number of the "Let's Clean Serbia" programmes, which have been broadcasted on a great number of televisions, where he informs the public about the great results of his work, but also promotes local DS officials throughout Serbia. Besides Minister Dulic, Nemanja Delic, the mayor of Sombor, also appears in the programme of 15 July 2010 on the web site, and Sasa Paunovic, the mayor of Paracin and DS cadre, appears in the programme of 5 August 2010. The list of DS officials appearing in these programmes is rather long, and includes Miroslav Krisan, the president of the Municipality of Kovacica, Zeljka Jurakovic, the direc-

tor of the Environment Protection Fund, Slobodan Kocic, the mayor of Leskovac, Vesna Martinovic, the mayor of Pancevo, etc.

Therefore, it can be said that "Let's Clean Serbia" was a great promotion of the officials taking part in it. Besides, there are all the legal premises that the government authorities should organize the cleaning of the country, but also punish those who pollute it, though voluntary cleaning should be organized by non-governmental organizations and not by the Ministry. The Ministry could have used the same money spent on the overly-expensive advertising campaign to cover the costs of the actual cleaning of the environment and the enforcement of the law; but it is not doing that because, it seems, the environment is not important either, but rather conducting a continuous political campaign is. In this way, party officials provide a political campaign for their party that they do not fund from the party budget, but from the budget of all the citizens of Serbia. Besides, a consequence of organizing such campaigns is creating influence over the media, which will not write critically about the fact that this Ministry always passes laws under urgent procedure, or explain the actual effects of the land conversion, or explain why some tycoons build even in protected zones of national parks, as in exchange they get money to advertise the campaign "Let's Clean Serbia".

Consequently, it is possible that 100 kilograms of dangerous medical waste is floating in the river Zapadna Morava, and no government institution accepts the responsibility for it, including the Ministry of Environment. Therefore, it is possible that the media, when they discover such alarming news, will later stop reporting about it or raising the question of the accountability, though it is very easy to discover the participants in this chain.

Besides the above stated, the Ministry of Environment and Spatial Planning has had a very "unusual" practice of engaging associations of citizens as companies, precisely for the campaign "Let's Clean Serbia". The association of citizens *Exit* had a contract for the production of a programme in the campaign "Let's Clean Serbia" worth 23.6m dinars in 2009, and 20m dinars in 2010. The Independent *Association of Journalists of Serbia*, which should represent the interest of the profession, was also engaged to "follow up the activities of the Ministry during the campaign "Let's Clean Serbia"" for an amount of 1.41m dinars in 2009 and 1.7m dinars in 2010.

More non-governmental organizations have been engaged to carry out some other activities in the area of media, and the *Media As-*

sociation ASMEDI was engaged in 2008 to co-fund the appendix to the weekly *Vreme*. In the same year the *Association of Journalists of Serbia* received half a million dinars for organizing the Eko Press Convoy.

For the same campaign the Ministry engaged *Orange Studio* in 2010 for an amount of 69.62m dinars.

➢ ***Infobiro and TV Frame***

While analyzing the documentation, the Council found out that two related agencies, *TV Frame* and *Infobiro*, were practically "covering" the activities of all the state institutions and that their income comes exclusively from the state institutions. Both these companies follow up the activities of the ministers and directors, and then pack the shot material, without a critical and analytical approach, as journalist contributions and post them on the closed web site www.infobiro.tv, from where televisions throughout Serbia download them free of charge. That is why those institutions which pay for this service (about 200,000 dinars monthly) can be sure that they will personally appear on the electronic media programmes.

The owners of *TV Frame* are Mile Balac and Bojan Trajkovic, and each of them owns a 50-percent share. The two of them also own a 50-percent share in the company *Infobiro*, where Sanja Ignjatovic and Ljubisa Paunovic own a quarter each. The services of *Infobiro* have been used by: the Ministry of Mining and Energy, the Ministry for Kosovo and Metohija, the Ministry of Telecommunications, the Ministry of Finance, the Ministry of Agriculture, the Ministry of Justice, the Ministry of Trade and Services, the Ministry of Labour, the Office for Developing Regions, the state-owned company *JKP Parking Servis* and the Agency for Small and Medium-Sized Enterprises. The Serbian Privatization Agency paid the largest monthly amount of 9,000 euros to *TV Frame* to follow up its work, and at certain time the agency could separately charge the travelling and stay costs abroad. From October 2008 to the end of the year, the Agency for Small and Medium-Sized Enterprises hired both these agencies, *Infobiro* and *TV Frame*, which were providing the same service – the follow-up of the activities. *TV Frame* produced the spots "The Tire Repairman" ("Vulkanizer") (1.21m dinars) and "The Hairdresser's Shop" ("Frizerska radnja") (1.68m dinars).

- *Agencies' income from state institutions*

Over the last three years *Orange Studio* has had the highest value contract with a state institution concluded in 2010 for an amount of

69.62m dinars; then follows *Morfeus Group* with an amount of 47.2m dinars in 2009. Both these agencies were hired for the campaign "Let's Clean Serbia". They are followed immediately by the agency *Adrenaline*, which made an income from *Telekom Serbia* of 32.9m dinars, then *TV Frame*, which in 2009 made only from the state authorities an income of 29.78m dinars. Then follows *Idea Plus Communications*, whose majority owner is the Slovenian company *Pristop Group*, with 18.79m dinars in 2008 for the Ministry of Health's campaign "Health Is Passed Along by a Smile"; then *Communis* (17.67m dinars in 2008), *Infobiro* (14.62m dinars in 2009), *Maxim Media* (14.37m dinars in 2008), etc.

When these amounts are compared with the total annual income of these agencies, it can be concluded that some of them operate only with the state institutions and not on the market. Thus *Morfeus Group* made an operating income of 55m dinars in 2009, and the contract with the Ministry of Environment and Spatial Planning alone was worth 47.2m dinars. *TV Frame* made an income of 41m dinars in 2009, while the value of its contracts with the state institutions was 29.78m dinars. *Maxim Media* made an income of 52,391,000 dinars in 2008, and the value of the contracts signed with the state institutions was 14.37m dinars.

RTS and RBA as services to the ruling elite

- **The Public Service RTS**

On a number of occasions over the last year the Anti-Corruption Council requested the documentation about the operation of the public service *RTS*, but received a partial response only in July and August this year. On 27 September 2010 the Council requested from the *RTS* director contracts concluded with independent production companies and individual authors in the period from 2007 to 2010, the contracts on business cooperation with the Eparchy of Backa, the companies *Communis*, *Caш Media Group, Film and Tone, Media Pro* and *Emotion Productions*, and copies of contracts for media advertising with marketing agencies which *RTS* concluded from 2007 to 2010, as well as all the contracts that were in force during this period and which had been concluded earlier. Since, in spite of the promises made by the director Aleksandar Tijanic, *RTS* has not delivered the requested documentation, the Council made an appeal to the Commissioner for Information of Public Importance. In spite of the Commissioner's Decision No. 07–00–02024/2010–03 of 29 November 2010 accepting the Council's appeal, and the submitted proposal by the Council for the enforcement

of the Commissioner's Decision of 1 February 2011, the *RTS* director did not deliver the requested data, but decided to pay a fine for non-compliance with the law. Consequently on 16 May 2011 the Council addressed the *RTS* Management Board. After a meeting between the Council's representatives with the new chairman of the *RTS* Management Board, Slobodan Markovic, held on 22 June this year, *RTS* started delivering parts of the requested documentation, making excuses that the material is too voluminous to be delivered in one lot. Most of the requested documents have not been delivered to us so far. A part of the Council's request to *RTS* was made in order to check the statements from the complaint sent to the Council by *United TV Experts – UTE*. It contained statements of serious abuses of office, corruption, conflict of interest, personnel manipulations, financial abuses, violation of the Labour Law, the Public Procurement Law, etc. The Council could not check some of the statements from the complaint because *RTS* kept silent.

The *RTS* director's non-compliance with the Council's requests to access information of public interest is not an isolated case. Specifically, according to the data received from the Office of the Commissioner for Information of Public Importance, in the period from 2008 to 2010 alone *RTS* did not comply with as many as eight Commissioner's decisions, by which the Public Service was ordered to deliver to the requesters information about whether it has the information and documentation requested by a number of associations, institutions and individuals.

It is stated in the complaint sent to the Council by *UTE* that *RTS* was awarding contracts to independent productions through a non-transparent procedure, which caused doubt that certain interest groups were making financial gain whose value is measured by dozens million of euros. Once a year tenders are formally announced for selection of programmes of independent radio and TV productions[9], but the results of these tenders are not disclosed to the public. A typical example of disputable cooperation with independent production companies is the contract with the production company *NIRA Film & Television Consulting* for the series "Time for Babies"[10] ("Vreme za bebe"), owned

[9] http://www.rts.rs/page/rts/ci/javniservis/story/621/%D0%9A%D0%BE%D0%BD%D0%BA%D1%83%D1%80%D1%81%D0%B8/254031/%D0%9A%D0%BE%D0%BD%D0%BA%D1%83%D1%80%D1%81%D0%B8.html http://www.rts.rs/upload/storyBoxFileData/2009/10/26/1100828/Nezavisne%20produkcije%20Javni%20poziv%202011.pdf

[10] http://www.rts.rs/page/tv/sr/series/20/RTS+1/64/Vreme+je+za+bebe.html

by Nebojsa Gagic, who is at the same time co-owner of the *Multikon Group* together with Dragan Djilas. It is a series which promotes childbearing in Serbia. However, according to the *UTE* statements, several months before awarding the contract to *NIRA Film & Television Consulting*, a series with identical contents had been prepared by an *RTS* team, on the order of the *TV Belgrade* director Nikola Mirkov. However, before the shooting started, the *RTS* director general Aleksandar Tijanic had concluded a contract with a private production company.

Besides non-transparent procedures through which contracts are awarded, the values of the concluded contracts are also disputable. For a 30-minute programme some production companies get from *RTS* a 3-minute commercial time compensation, and some get for similar productions unreasonably high money amounts. According to the documentation delivered to the Council by the *RTS* director after the intervention of the Management Board, the highest financial compensation per programme was paid to the production company *Emotion Production* for the programme "48-Hour Wedding Party" ("48 sati svadba"). The contract for the transfer of the TV right, concluded on 19 June 2006 between *Emotion Production* and *RTS*, provides that *RTS* should pay *Emotion* for the right to broadcast the 104-episode series 12,948 euros per episode, and an annex for the extension of the validity of the contract for another 104 episodes was concluded on 29 June 2007. Additionally, according to the Contract, *Emotion* has the right to commercials and advertising time, which is specified by another contract, which has not been delivered to the Council. *Multikom Group*, owned by Dragan Djilas, had been a co-owner of this production until recently with a 49-percent share. According to the *UTE* statements, *RTS* pays for independent productions' series feature programmes even more, as much as 80 to 130 thousand euros per episode.

Since 2006 *RTS* has also had business cooperation with the production of the Eparchy of Backa of the Serbian Orthodox Church (SOC). The contract from 2006, delivered to the Council by *RTS*, provides that 60 percent of the total annual budget for the programme "The Church Calendar", which amounts to 187 thousand euros, should be paid in cash and the rest in advertising time. A five-year agreement for cooperation on production and broadcasting of the religious programme was concluded between religious communities and *RTS*, which provides that the SOC Eparchy of Backa should be the producer again, but the financial particulars of this deal are regulated by a separate contract, which has not been delivered to the Council. The photocopy of this Contract, which regulated the financial value of this programme

from 15 May 2007 to 15 May 2008, was delivered to the Council by the UTE. The Contract provided that the RTS should pay 24.344.340,80 dinars to Backa Eparchy for one year production of the programmes "The Religious Calendar" and "The Religious Mosaic". Besides the contract the UTE delivered to the Council two bills which Backa Eparchy sent to the RTS on 17 October and 1 November 2008, the amount of the bills were 2.028.695,00 dinars and 1.478.049,26 dinars.

Some members of the *RTS* Management Board, who make decisions on the appointment of the director of this medium, also appear as authors of programmes or are related to private production companies which cooperate with *RTS*. Thus Dr. Predrag J. Markovic, a member of the *RTS* Management Board and an official of the Democratic Party (DS), was also the author of a number of quizzes for which he received, besides the high monetary compensation he gets as a member of the Management Board, fees through the company *Film and Tone*, owned by his father Jovan Markovic. According to the received documentation, the company *Film and Tone* has cooperated with *RTS* since 2008 on the production of the quiz "The High Voltage" ("Visoki napon"). The annual compensation to the team of authors grew from year to year, from 4m dinars in 2007 to 7m dinars in 2010, while *RTS* also paid that company an amount of about 2m dinars for the licence. *RTS* has also delivered to the Council some annexes to contracts which show that this company also sold films to *RTS*, but the basic contracts have not been delivered.

Dusan Stokanovic, also a member of the *RTS* Management Board, was the leader of the production preparing the programmes "The Religious Calendar" ("Verski calendar") and "The Religious Mosaic" ("Verski mozaik"), for which *RTS* pays significant fees through the Eparchy of Backa. Among its employees, *RTS* has owners of private productions; for example, Nenad LJ. Stefanovic, the responsible editor-in-chief of the *RTS* informative programme, is one of the ten owners of the company *Vreme Film*, which has concluded valuable contracts for the production of documentary-informative programmes for *RTS*.

The documentation delivered to the Council shows among other things that some contracts with production companies provide for compensation, not in money, but in seconds of advertising time. The research conducted by the Council among some small production companies hired by *RTS* in this way, showed that these companies are not often able to sell their seconds of earned advertising time, but they are obliged to sell them at a significantly lower price than their realistic price to big marketing agencies behind which are party officials

and persons related to them. Representatives of one of the interviewed production companies stated that they had to sell their seconds of *RTS* advertising time to a big marketing agency at a price even ten times lower than the price foreseen by the relevant *RTS* pricelist. On the other hand, the mentioned contract with the production company *Emotion Production*, behind which Dragan Djilas had been until recently, provides that *RTS* pay for the right to broadcast 104 episodes of the series "48-Hour Wedding Party" ("48 svadba"), 13 thousand euros per episode. In other words, the same persons who stand behind the marketing agencies that buy off the seconds of advertising time from small production companies at unreasonably low prices get paid in cash and not in seconds of advertising time.

According to the statements in the *UTE* complaint, *RTS* has for years drastically violated the Advertising Law. However, only in 2011 the RBA started submitting charge sheets against media, including *RTS*, for violation of the Law on Advertising and Broadcasting. In 2010 the most serious misdemeanor in the work of *RTS* established by the RBA referred to the protection of the Serbian language in the programme, as it often happened that inscriptions are written in the Latin script, but it is claimed that *RTS* fulfills all the supervised programme obligations. At the same time *RTS* does not publish data about its business operation, realization of the programme production, the share of the subscription and advertisements in its income, its expense, salaries of the employees, how business and programme decisions are made by the management bodies, etc.

In the presentation of the biggest *RTS* financial problems in its complaint, the UTE especially emphasized the organization of the Eurovision Song Contest 2008. The contract which *RTS* delivered to the Council, concluded between *RTS* and the agency *Communis* for the realization of the Eurovision Song Contest 2008, is worth 24,723,000 dinars, which is approximately 300,000 euros at the rate of exchange prevailing at the time. A precise financial report on this event has never been presented to the public. The UTE also states the existence of an increasing indebtedness of *RTS*. Both long-term and short-term liabilities have been constantly increasing. As of 31 December 2008 the *RTS* short-term liabilities exceeded its current assets by 1.484b dinars. All this indicates great uncertainty regarding the material business operation, which raises justified suspicion that *RTS* will not be able to operate in future in accordance with legal principles. *RTS*'s poor business operation worsened in 2009, but the financial reports for 2009 and 2010 have not been published to date.

RTS is funded from public revenues and it is an institution which has a special role in the social, cultural and political life of Serbia. The stated problems are so much bigger because *RTS*, as a public service, has a greater responsibility than other media and commercial televisions in the creation of public opinion and representation of the general interests of the citizens. However, the *RTS* management's refusal to comply with the Law on Free Access to Information of Public Importance and enable the public to see how public funds are spent, puts into doubt its ability to fulfill the most important tasks of this public service, one of which is the fight against corruption. An efficient fight against corruption, which is a priority interest of the citizens of Serbia, requires unanimous support from the public and the civil society, which can be achieved only through the media, primarily through the public broadcasting service. However, the question is how can *RTS*, which operates non-transparently itself, contribute to the fight against corruption? That is probably why programmes of the public service very rarely include investigative, analytical and critical contents.

- **Republic Broadcasting Agency (RBA)**

The (RBA), for which it can be said that it has never been really independent, but rather has worked under the constant influence of political parties, has significant responsibility for the present situation in the media sector in Serbia. The first cases of disputable decisions on awarding national licences for broadcasting programme (*TV BK, RTL*) are known, then non-compliance with the Supreme Court's decision, then the unlawful Obligatory Instruction to *RTS* to broadcast the Serbian Assembly sessions, as well as a series of other RBA actions, such as approval of obvious and forbidden media concentrations. Thus, instead of defending the principle of the transparency of media ownership, RBA has contributed mostly to the creation of the atmosphere of concealed interest in the electronic media because it is exactly the RBA Council which has "in its hands" appropriate mechanisms for the prevention of forbidden media concentration in the media sector. During the past three years RBA has approved at least two disputable concentrations of media ownership in the case of *TV Avala* and *RTV B92*. As could be seen, out of the eleven national broadcasters there are nine with non-transparent ownership. In the July 2011, when the Council finished the first Draft Report and delivered it to the relevant organizations, associations, and individuals with appeal to make the comments, the RBA published on its web site the data about owner-

ship of the radio and TV stations with national coverage. Even though the RBA published certain data, which were not officially published before (even though that information were given to the public by unofficial sources), the media ownership is still non-transparent according to the domestic laws and the recommendations of the Council of Europe, which provide that the transparent ownership prevents the creation of monopoly in the public information sector, and to enable the judgment on the information and ideas presented by the media. The doubts about illegal media concentration in the cases of TV Prva/RTV B92 and TV Avala/TV Pink after the RBA has published the data on the ownership of the media were not confirmed nor eliminated. It is also not clear from the data on the RBA web site does a businessman Predrag Rankovic Peconi control Happy TV and Happy Kids TV, and without that information a judgment about their programmes can not be created.

The first problems in the work of this institution started with the first election of the RBA Council members in April 2003. A specific problem in the work of this institution is also the fact that the Broadcasting Law has been amended several times. According to the original solution, the Parliament of Serbia elected eight members to the Council following the proposal of authorized proponents: the Government of the Republic of Serbia (1), the Parliament of Serbia (1), the Parliament of Vojvodina (1), the Executive Council of Vojvodina (1), the University chancellors (1), associations of broadcasters, journalists and other professional associations (1), domestic NGOs (1), and churches and religious communities (1). The ninth member was elected by the Council members themselves, but he had to be from the territory of Kosovo and Metohija. It proved in practice that it was not clear who nominated candidates of the Council members, but it was most important who elected them – deputies of the ruling parties.

Three RBA Council members, Nenad Cekic, Vladimir Cvetkovic and Goran Radenovic, were elected in April 2003 contrary to the procedure, which caused a blockade in the work of the Agency as consequently some of the elected RBA Council members resigned (Snjezana Milivojevic and Vladimir Vodinelic). The foreseen nomination procedure, according to which the nominations, together with the CV data, must be published a minimum of 30 days before the election, was violated, as it was not done in the procedure of nomination of Cekic and Cvetkovic. In the case of Radenovic, who was elected as someone who was to live and work in Kosovo (which was a statutory condition), it

was established that he had left the Province long before that. Consequently the RBA Council always worked in an unlawful atmosphere and, therefore, the first RBA decisions were always disputed.

Owing to the previous problems, the Law was partially amended in 2004 regarding the procedure of the election of the RBA Council members and the simplification of the election procedure; these amendments did not include the request of the media organizations that the prevailing influence of the state authorities on the election of the Council members be reduced, as it still does not provide independence in the work of RBA. The Law amendments only changed the wording referring to the authorized proponent nominating candidates for RBA Council members, so that instead of the "Government of Serbia and the Parliament of Serbia" the authorized proponent became the "responsible parliamentary board", which boiled down to almost identical political influence. Instead of the Government and the Parliament of Serbia, government bodies still directly nominated four RBA Council members (three by the responsible parliamentary board and one by the Parliament of Vojvodina), concealed behind the term *parliamentary board*, where the ruling coalition always has a prevailing influence.

The politicization of the election of the RBA Council occurred again at the beginning of 2009, when the term of office of some members expired and it took almost one and a half years to have new members elected. A specific problem was the fact that the first RBA Council members had not been elected for the same term of office of six years, as foreseen by the Law. It was clear in March 2009 that all the deadlines for the election of the members had been missed, but the solution was not in sight. Following the proposal of the Parliament of the AP Vojvodina, the University, the religious communities and NGOs, the RBA Council members were elected by the end of that year (Goran Karadzic, Vladika Porfirije, Svetozar Stojanovic and Goran Pekovic), where authorized proponents – NGOs and the professional media associations – nominated more than the foreseen number of candidates. Specifically, the Broadcasting Law provides for the nomination of two candidates for each member, while on their candidate lists they had three and four names and, therefore, Serbia's Parliamentary Board arbitrarily elected two candidates from each list, which caused great dissatisfaction with the proponents. This again created problems with the election of Council members representing journalists, and the election turned into a political mockery.

For months the RBA Council was incomplete, and at certain time it had only five members, instead of nine, because in February 2011 the term of office expired for Nenad Cekic, then for Aleksandar Vasic and Vladimir Cvetkovic, while Svetozar Stojanovic died in May 2010. At the beginning of April 2011, Goran Petrovic, a lawyer from Kragujevac, was elected. According to the media reports, his two previous employments had been at the Health Centre of Kragujevac and the Pharmaceutical Institution. Petrovic was formally nominated by the University Conference of Serbia, but he came to the RBA Council as DC cadre, who worked as a journalist only in his youth for *Views* (*Pogledi*). His counter candidate was Dr. Natasa Gospic, who had graduated from the Electronics and Telecommunications Department of the Faculty of Electrical Engineering in Belgrade. She has published two monographs and more than 90 professional and scientific papers in the area of the development of telecommunications and information society. However, the professional criteria were not decisive this time either. All the described cases significantly burdened the work of RBA affecting the independence of the work of this institution, which, as it turned out, depended a lot on political parties.

RBA had most of the controversies in its work regarding the disputable award of licences to the national broadcaster for broadcasting programmes in 2006. On that occasion *TV BK* was practically closed because of the publicly disputed decision not to award it a national frequency licence. The licence was not awarded to the German company *RTL* either, nor to *TV 5* from Nis. *TV BK*, owned by the domestic tycoon and then-president of the political party the Force of Serbia Movement, Bogoljub Karic, formally lost the licence to broadcast its TV programme because of political bias. The programme of this TV station was stopped by force the very next day after the decision was made, when police invaded the premises and stopped the broadcasting of the programme. In spite of the ban, *TV BK* continued broadcasting its programme via satellite and organized protests, but it ceased these activities in 2007. In October 2008 the Supreme Court of Serbia overturned RBA's 2006 decision on awarding the licences for broadcasting programmes on the national network by which the work of *TV BK* was forbidden; however, RBA not only refused to comply with the Court decision, but issued a new banning decision. After that, RBA has never issued a similar decision banning the work of any medium; it has been conducting a very weak penalty policy towards broadcasters.

The German *TV RTL* did not get a licence in 2006 because of the majority foreign capital, but at the same time a licence was awarded

to *TV Fox*, though it was known that American capital prevailed in its ownership structure. That decision was also overturned by the Supreme Court of Serbia in July 2007, when the president of the RBA Council, Nenad Cekic repeated that they would not comply with Court's decision.

TV5 from Nis did not get a licence at the first tender in 2007 in spite of the fact that it was the regional TV channel with the greatest viewer rating in Serbia. It was rejected because of the ownership share of Olivera Nedeljkovic, Bogoljub Karic's sister, but at the next tender a year later, it met all the requirements to get the frequency as it had got rid of Nedeljkovic's capital.

At the same tender licences were awarded to *TV Kosava* and *TV Happy*, which had not existed before, and whose ownership structure proved to be disputable later on as it was related to some domestic businessmen. Subsequently it was published that *TV Pink* gave an 18-million dinar loan to *TV Kosava*, but it did not affect RBA'a decision to award a licence to this TV channel.

On that occasion a national licence was also awarded to another newly-established television – *TV Avala*, which is co-owned by businessman Danko Djunic and whose ownership structure is still disputable, or insufficiently clear.

Besides the mentioned problems with national frequencies, there was a certain number of disputable decisions made by RBA related to local licences in Apatin, Subotica, Backa Topola, Kovin, Prijepolje and other places, which were often made in accordance with the local political needs of the city assembly majority of the relevant town or city. It was too late for *Radio Apatin*, whose appeal was accepted by the Administrative Court last year, for the decision arrived too late as the medium had already ceased its work.

Most of the international organizations, such as OSCE, the Council of Europe and the European Commission expressed their serious concern because of the procedure according to which licences were awarded, which was assessed as biased because it was conducted with inappropriate application of the rules and criteria. The European Commission specifically indicated the lack of transparency in the process of decision making by the Republic Broadcasting Agency (RBA). Nevertheless, most of RBA's disputable decisions have not been changed so far.

In 2008 the Constitutional Court of Serbia found that the RBA Council's Obligatory Instruction regarding the broadcasting of the Parliamentary sessions by *RTS* was unconstitutional and unlawful because

of the transgression of competence by the Agency. Specifically, RBA obliged *RTS* to broadcast Parliamentary sessions at the times specified by the Rules on the Work of the Parliament, for the purpose of exercising special obligations in public interest. Two months later, RBA replaced the Obligatory Instruction with a Recommendation by which the same obligations are recommended to *RTS* for the purpose of exercising public interest in the area of public information.

The Report on the Work of RBA 2009 speaks to another problem with the work of this agency. In 2009 this institution made an income of about 457m dinars (€ 4,160,000) from licence fees, out of which an mount of 318.5m dinars (€ 2,905,000) was paid to the officials of RBA itself, while the remaining amount of 139.3m dinars (€ 1,270,000) was transferred to the Budget of the Republic of Serbia. Media organizations stated on a number of occasions that it is impermissible that the Agency itself decides how much money, received from licence fees, would be spent for its own needs and how much would be returned to the budget, while at the same time it does not participate in funding media development projects. When making an analysis recently, the Anti-Corruption Council found out that RBA had hired companies in a non-transparent way to carry out various types of research for the needs of the work of the Agency. Thus one of these companies, *News Pro* from Subotica, closely related to RBA deputy president Goran Karadzic, made some analyses of the media market of the local and regional broadcasters and *RTV* programmes. The owner of this company from Subotica is Velimir Kostadinov, a full-time journalist of *Vojvodjanski magazin* (*Vojvodina Magazine*), whose owner and editor is Goran Karadzic himself. At the same time Kostadinov holds the office of deputy editor of *TV Super* from Subotica, but in 2009 Karadzic used him as his counter candidate for a member of the RBA Council, because the proposal of the Parliament of Vojvodina was to have names of two candidates.

RBA normally fails to react in cases of drastic jeopardizing of public interest by showing violence in reality programmes. Swear words, violence and insults are everyday features of these programmes, though according to Article 68 of the Broadcasting Law, broadcasters "must not broadcast programmes whose contents can be harmful for the physical, mental or moral development of children and youth, should clearly mark such programmes, and if they broadcast them, they should do it only between 24.00 and 06.00 a.m.".

Despite everyday violation of the Advertising Law, until the end of 2009 RBA had not submitted any charge sheets or managed to make televisions limit their advertising time in accordance with the Adver-

tising Law and stop with concealed advertising, and despite the fact that fines range up to 1m dinars. According to the latest data, the situation has changed a little this year and in the first half of 2011 RBA submitted a greater number of charge sheets. According to RBA data, national televisions violated the Advertising Law in that period 2,123 times. The record holder is *TV Prva*, which did not comply with the Law 539 times. Then comes *RTS 1* with 405 times, which is followed by *B92* with 338 violations. *TV Pink* had 315 violations, *TV Avala* 93 and *TV Happy* 91.

The Broadcasting Law gives open hands to the RBA Council to regulate the media scene by starting with warnings, and if the television stations do not respond, to revoke their licences temporarily or permanently. RBA may order the following measures to broadcasters: warning, reminder, temporary or permanent revocation of the broadcasting licence, but it has been proven that RBA is ready to impose the most drastic punishment only when it is in a political interest.

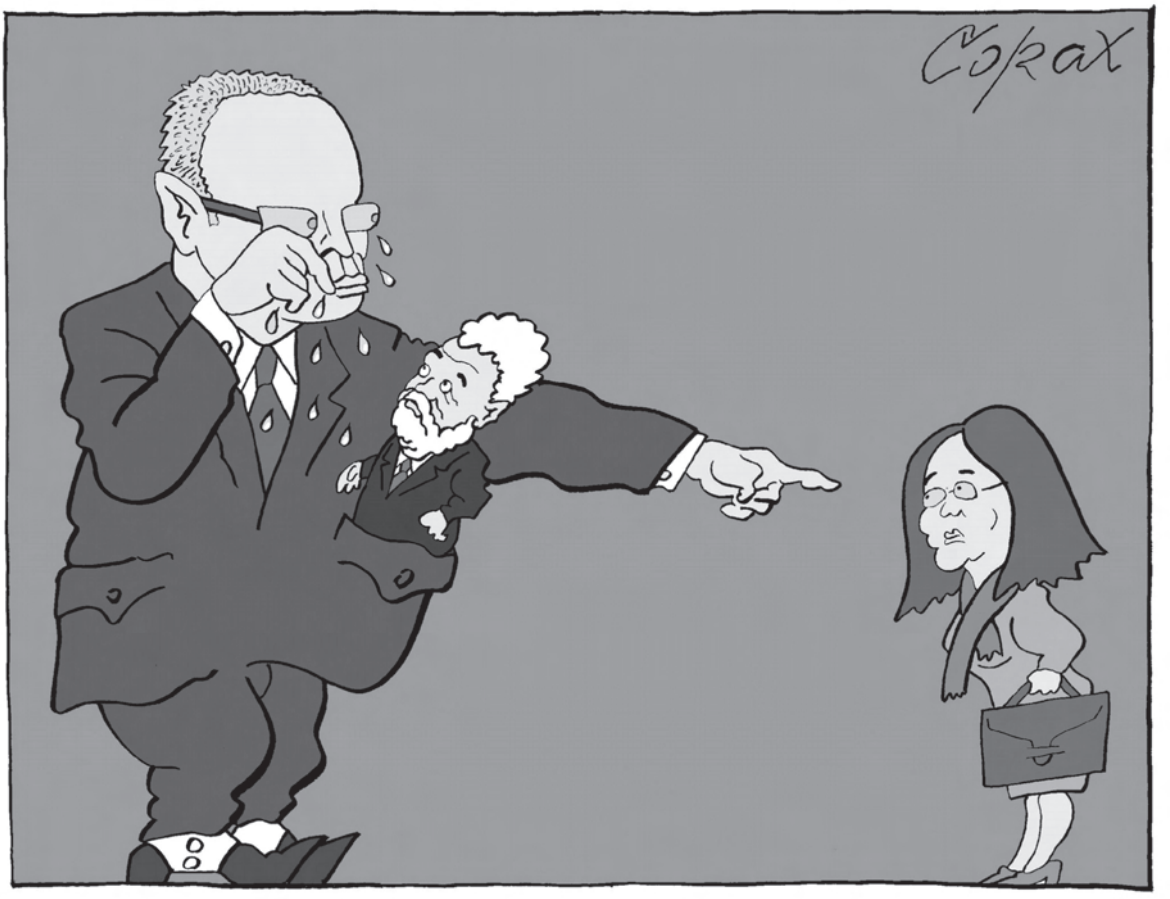
Recommendations:

- Data on the actual media owners in the public media register should be made public, especially in cases where the ultimate owners are from an off-shore zone or where the real owners are hidden behind the individuals who appear as formal owners in the competent registers
- Commission for Protection of Competition, the Republic Broadcasting Agency and other competent bodies in accordance with their competences should monitor and regulate the level of media concentration related to the ownership, programme diversity, concentration on the marketing market, and also they should investigate and encourage media pluralism, diversity and quality of programme according to the European union norms.
- Budgets of state-owned institutions should be limited regarding the use of the budget for advertising and promotion, and state institutions which violate the Advertising Law should be sanctioned.
- Regular public procurement procedure should be prescribed for the services of providing information, production of *RTV* programmes and services in the area of relations with media,

because transparent selection of tenderers can be ensured only in this way.

- Article 74 of the Broadcasting Law stipulates that the institutions of public broadcasting service of the Republic of Serbia, the autonomous provinces, as well as the local and regional broadcaster of the local communities, which are mostly owned by state, are obliged to made available 10 percent of the annual amount of programme to the independent radio and TV productions. The independent productions selection process should be transparent and according to the exact procedure based on criteria which are consistent with the public service role of the broadcaster and not with the commercial profit (some shows created by independent production, for example, 48-Hour Wedding Party)
- State institutions should in their regular reports consolidate all forms of cooperation with media and present them as advertising in media, and not as non-defined specialized services, research, and other classifications which imply simulated jobs.
- Commissioner for information: Information on business cooperation of the bodies of public authorities and media should be defined as obligatory contents of the Information Book on the Work of Authorities so that transparency may be enhanced in this area.
- The Government of Serbia should publish a consolidated tender for procurement of video recording services and post it on its Internet page, or establish a video recording department within its Office for Cooperation with Media
- The Government of Serbia should publish a consolidated tender for procurement or establish a press clipping department within its Office for Cooperation with Media.
- RBA and *RTS* should publish the official results of the tender for selection of *RTV* production programmes, and the financial statements, every year.
- RBA and *RTS* should prevent RBA Management Board and Council members from participating as programme producers.

Yours faithfully,
President
Mrs. Verica Barać


Corax

REPORT ON THE SALE OF THE COMPANY *DELTA MAXI*

Report Summary

The sale of the retail trade company *Delta Maxi* was agreed upon at the end of July this year. The Buyer is a well-known Belgian trade company which appears on the market under the name *Delhaize Group*. A total sales price of 932.5 million euros was agreed upon, including *Delta*'s debts of an unknown amount, which is less than 318 million euros.

Though these are private companies, the social consequences of this sale are significant, especially considering the corruption level in the country. At the same time the following facts, about which the Anti-Corruption Council has reported comprehensively, are important:

- the price of the *C-Market* shares was fixed by the famous Memorandum, which was concluded under the auspices of the Prime Minister, in accordance with *Delta*'s interests (purchase of shares from small shareholders);
- the merger of *Primer C* and *C-Market* was carried out without an approval by the Commission for Protection of Competition (hereinafter the Commission);
- the Commission had no Government support in preventing the creation of a trade monopoly. What is more, it was constantly threatened by the Law amendment which would establish a new (cooperative) Commission;
- no court in the country wanted to consider the arguments of the Commission or the small shareholders, which certainly would not have been possible without the pressures of the executive power;
- for years the state authorities ignored the widely known fact that *Delta* was not systematically paying its debts to its suppli-

ers, thus creating a non-solvency chain which jeopardized the operation of a great part of the economy.

At the beginning of July this year the Council of the Commission for Protection of Competition issued a decision by which it approved the purchase and at the same time legalized the monopoly created on the Belgrade market. This time the Commission linked the incompatibles – the request of *Primer C* from January 2006 for approval of the concentration created by the purchase of the *C-Market* shares and *Delhaize*'s application for concentration from March 2011. The same decision ignored all the findings of the Commission's previous members and even the results of the ordered study, which showed that the offer concentration level on the Belgrade market was high (higher than 1800 points according to the Herfindahl–Hirschman Index). The observed abuses of the dominant position made systematically by *Delta* in the previous period were also ignored.

The Government must ensure the security of the property rights. The first step on this path is to cut the "Cyprus Network" by unveiling the network of companies and individuals who illegally took money out of the country and who are bringing it back in form of "foreign investments", violating thereby many regulations and procedures. Besides, it is necessary to amend the legal norms relating to the registration of business companies, money laundering, conflict of interest and the relevant market.

Sale Of The Company *Delta Maxi*

At the end of July the public was informed that the sale price of the retail trade company *Delta Maxi* (hereinafter: *Delta*) had finally been agreed upon. The Buyer is the well– known Belgian trade company which appears on the market under the name of *Delhaize Group* (hereinafter: *Delhaize*). The total agreed sale price is 932.5m euros, including the amount of *Delta*'s unknown debts, which are less than 318 million euros.

The negotiations leading to the conclusion of this deal lasted for quite a long time. Though these are private companies, state officials were also included in the negotiations. The deal was confirmed by the statements made by President Tadic and the Belgian Prime Minister Leterme at a press conference held in Brussels in July last year, when the intended initiative of the Belgian company was announced.

It is certainly good that the president of the Republic of Serbia actively followed up the negotiations, though it is not within his competence, as *Delta* has accrued huge debts which have serious macroeconomic consequences, and as the owner of that company has been involved in a number of business scandals which indicate possible corruption in the highest circles of the power, about which the Anti-Corruption Council has informed the Government and the public in detail (Reports on *C-Market, Belgrade Port* /*Luka Beograd*/, conversion of land in New Belgrade, etc.).

The Government has not taken an official view either regarding the Council's report, or regarding the recent sale of *Delta*, though it is responsible both for combating corruption and conducting the macroeconomic policy.

The Council believes that the fight against corruption must be conducted primarily against large-scale corruption, which is destroying our economic and political systems. So far no case of large-scale corruption has been concluded by the pronouncement of a final court verdict, which undoubtedly speaks to the untouchability of the corruptionists, who are positioned high enough in the social hierarchy. A direct consequence of such a policy is the weakening of wide public support for democratic political order.

Another reason the Government must not keep its arms crossed and ignore large-scale corruption is the international public. Foreign investors are aware of the insecurity of property rights and they obviously steer clear of Serbia, especially with the real sector investments. Besides, the European officials point out the fight against corruption as one of the basic preconditions for joining the European Union (EU). They simply do not wish to have among themselves a country where corruption is more pronounced than in Bulgaria and Romania.

What is the connection between the sale of *Delta* and the fight against large-scale corruption? Though this is the sale of a private company to a foreign shareholding company, the social consequences are multiple. *Delta* is a large retail trade company, which, shortly upon its establishment, acquired a monopolistic position, primarily on the Belgrade market, by violating numerous legal norms and procedures. In doing this, in crucial moments it had support from the Government top officials. We shall remind you of only several events about which the Council has reported in detail:

- the price of the *C-Market* shares was fixed by the famous Memorandum, which was concluded under the auspices of

the Prime Minister, in accordance with *Delta*'s interests (purchase of shares from small shareholders);

- the merger of *Primer C* and *C-Market* was carried out without an approval by the Commission for Protection of Competition (hereinafter the Commission);
- the Commission had no Government support in preventing the creation of a retail trade monopoly. What is more, it was constantly threatened by an amendment to the Law, by which a new (cooperative) Commission would be established;
- no court in the country wanted to consider the arguments of the Commission or the small shareholders, which certainly would not have been possible without the pressures of the executive power;
- for years the state authorities have ignored the widely known fact that *Delta* has not been systematically paying its debts to its suppliers, thus creating a non-solvency chain which jeopardized the operation of a great part of the economy.

The Report we are submitting to the Government first reiterates the most important facts which have led to the present situation. Then it analyzes the Commission's Decision by which the acquisition *Delta* by *Delhaize* was approved, and then it analyzes the recently accomplished sale. On the basis of the analyzed case, we finally make recommendations to the Government about what steps should be taken in order to curb large-scale corruption.

How Have We Arrived at this Situation?

Delta was established in 2004, with the aim to compete for the establishment of a monopolistic position on the Belgrade retail trade market of foodstuffs and consumer goods. It is often stated in public that Miroslav Miskovic is the founder and owner of the company. However, the official documents acquired by the Commission indicate that *Delta* is owned by the Cypriot company *Hemslade Trading Limited*, which was established in 1991, immediately upon the expiry of Miskovic's term of office as deputy prime minister of the Serbian Government. Today *Hemslade* is 100% owned by the phantom company from the Virgin Islands *Hitomi Financial Limited*, whose founders and owners are concealed from the public.

Market characteristics

At the time when *Delta* was established, the market was dominated by two companies – *C-Market* and *Pekabeta*, where the first competitor was much stronger than the latter. The ratio of the number of shops was 179 to 66, while the difference in income was still higher in favour of *C-Market* – 16 billion dinars compared to 4.7 (in 2004). *C-Market* had one-third of the retail space in Belgrade and its share of the total share in the relevant market was approximately the same. To a certain degree, three more companies – *Jabuka, SiMarket* and *Rodic* – had significant market shares. *Mercator* showed its clear intention to expand on the retail trade market, and some other foreign competitors (*Cora, Carrefour, Metro*...) announced their arrival, but they were mainly interested in opening hypermarkets (stores exceeding 2000 m2).

The market was asymmetric, with undertakings of different strength, where the dominant company (*C-Market*) aggressively fought to increase its share. If the Government had tried to protect the interests of the consumers and producers in such a situation, it would have encouraged competition, primarily by ensuring free entry of new competitors. Moreover, competition of retail trade companies is beneficial for the entire economy. It lowers the selling prices, which is in the consumers' interest – the consumer surplus (the difference between the price the consumers are ready to pay and the price they actually pay on the market) is increased. On the other hand, the competition among the retailers pushes up the prices obtained by the producers (suppliers) and it stimulates production. Of course, the reduction of the prices paid by end consumers and the increase of prices obtained by suppliers is possible only by the reduction of the retailers' profit (margins and discounts).

Unfortunately, instead of encouraging competition and working thus in the interest of the economy and the households, the political elite opted for the interests of a small number of individuals, popularly called tycoons. The answer to the question of why things have been developing in this way certainly requires a more comprehensive analysis, but the course of events that followed certainly indicates the existence of a clear connection between political elites and tycoons, and it puts into the limelight the non-transparent funding of political parties. And the height of the irony is the fact that the governments which took measures in the interest of tycoons were controlled by different democratic parties.

Takeover of C-Market

At the time of the establishment of *Delta*, the employees of the biggest retail trade company, *C-Market*, were its majority owner. They acquired the shares in the privatization procedure, by the application of the 1991 Law on the Conditions and Procedure for Transformation of Socially-Owned Property into Other Ownership Forms. A relatively large number of shareholders posed an objective obstacle to acquiring cheaply the majority package of shares. However, the director of the company, Slobodan Radulovic, opted for a tested method of ownership concentration, which had proved successful on many occasions with the application of the regulations from the 1990s, which provided for privatization through the purchase of employees' shares. By pressuring and threatening the employees, he forced them to sell him their shares at a low price. The employees were simply put into a dilemma: either to keep the paper (the share certificates) which did not bring them any profit (no dividends were paid) or lose their job, or to keep the job and sell the shares to the director at a relatively low price.

In its documentation the Council has numerous testimonies of the owners of the company about the behaviour of the *C-Market* director and his relationship towards them. According to his own admission (statements he delivered many times to the Council and the wider public), Radulovic made his ownership concentration plan together with Milan Beko, unaware what would come to light later on – unaware that Milan Beko was acting in the interest of Miroslav Miskovic.

The plan could not be simply realized as in the meantime the Law on Securities Market had been changed and the procedure for the purchase and sale of shares on the stock exchange had been made significantly stricter. To make the matters worse, Slovenian *Mercator* announced its readiness to submit its bid for the takeover of *C-Market* shares in accordance with the Law. In such a situation the tycoons decided to act in two directions: they initiated a public campaign "against the sale of the market to Slovenians", and the sale of *C-Market* shares was forbidden by the Commercial Court, despite all legal norms.

The Commercial Chamber of Serbia, whose president was Slobodan Milosavljevic, later on also a long-time minister of trade, organized the "defence" of *C-Market* by creating a consortium of the largest Serbian companies (which were, of course, led by *Delta*). The task was to prevent *Mercator* of taking over in any way the Serbian company. It was announced that the companies would raise money for the "patri-

otic" purchase of the shares, "young workers" and "future shareholders" organized street protests.

It is certainly clear that the strong media campaign and extremely biased court decisions could not be realized without the involvement of the political elite. Numerous comments in the media confirm this, which, as a rule, denied *Mercator* the right to obtain the desired shares through free market competition. Milosavljevic stated that the national market was the most valuable asset and that the "businessmen still have a chance to preserve a part of the market for themselves by establishing a consortium". Nevertheless, there were rare statements about possible benefits for the shareholders and the rest of the economy. However, the initiative of the Government itself confirms more than anything else the existence of political interference.

Memorandum imposing the price of the shares

In August 2005 the Government secretary general, Dejan Mihajlov and the chief of the Prime Minister's Cabinet, Aleksandar Nikitovic, initiated a meeting at which Miroslav Miskovic, Slobodan Radulovic, Milan Beko and Danko Djunic resolved all the dilemmas in connection with the purchase of *C-Market* shares. It was agreed that a price of shares in accordance with *Delta* interests be paid to small shareholders, and that the procedure of the purchase of the shares be carried out by Radulovic's company *Primer C*. Immediately upon the takeover of the shares, the ownership of *Primer C* was transferred to the Luxemburg based company *Novafin*, controlled by Milan Beko, which is otherwise owned by the Cypriot company *Hemslade*. The agreement was made in writing under the title of "Memorandum of Understanding" signed (and initialled on each page) by the main protagonists.

After the successfully concluded agreement, a cocktail party was organized for Prime Minister Vojislav Kostunica, who expressed his satisfaction because *C-Market* would "remain in Serbian hands". This was confirmed by statements made by Milan Beko (before the court) and Slobodan Radulovic.

On two occasions the Council submitted a copy of the Memorandum to the Government, which never responded to it. The Prosecutor for Organized Crime stated to journalists that the original of the document was not accessible, a copy has no evidence value and, therefore, there was no basis for the initiation of a proceeding. Besides, he expressed his doubt that the meeting had been held at all.

Agreements on imposing prices and price-fixing are forbidden by all anti-monopoly laws. At the time the Federal Anti-Monopoly Law, which also forbade price fixing, was effective in Serbia.

It is normal that the buyer and the seller agree on a price suitable for both parties through negotiations. However, if two or more market undertakings, out of which some even do not participate in the sale or purchase transaction, fix a price (in this case the price of shares) to be paid to the seller who does not take part in the agreement, then it is an imposed price. Such agreements are forbidden, and if they are made anyhow, they are considered null and void. The parties to such an agreement must compensate the damage sustained by the third party, pay penalties many times higher than the caused damage, and some legislations of EU member states also provide for an imprisonment penalty for participants and instigators of price-fixing agreements.

However, in this case the implementation of the provisions of the Memorandum proceeded according to plan. By the beginning of December 2005 the shares of the employees had been bought off, the fixed price had been paid out with money whose origin has never been established. The Directorate for the Prevention of Money Laundering did not even try to establish the origin of the money in spite of the fact that *Primer C* had no turnover in the year preceding the purchase of the shares. A total amount of 45 million euros was paid for 74.59 percent of the capital of the company. The only remaining thing was that the ownership of Radulovic's company be transferred to a company controlled by Beko. For this they needed the Commission's approval and that created a problem.

Forbidden concentration

In July 2006 the Council of the Commission established that *Hemslade* was not only the owner of *Novafin*, which was to take over *Primer C*, and the *C-Market* shares, but that it was also the owner of *Delta*. By the foreseen transaction *Hemslade* would become the owner both of *C-Market* and *Delta*, and thus a dominant company would be created with a market share of over 55 percent (40 percent is the legal limit for a dominant position) and, therefore, the Commission refused to allow the merger.

As the Decision was final, *Primer C* initiated an administrative proceeding before the Supreme Court of Serbia. Besides the stated positions, the plaintiff submitted, as their arguments, two studies ordered

by *Delta*. One of the studies was prepared by a group of professors from the Belgrade Faculty of Law (Vesna Besarovic, Mirko Vasiljevic, Gaso Knezevic, Boris Begovic, Dragor Hibner and Vladimir Pavic), and the other one by the Serbian Chamber of Economy and *Conzit* (a family company owned by Slobodan Milosavljevic). Both studies challenged the findings of the Commission, which was accepted by the Court.

By its verdict from September 2007, the Supreme Court quashed the Decision for formal reasons, but also because of "incompletely established facts". The enclosed studies "confirm the points of the claim" and, therefore, the Court ordered the defendant to eliminate the shortcomings in a renewed proceeding.

In November of the same year (2007) the Commission issued a new decision. By this Decision it refused again the request for the concentration. It was established by a survey of consumers that the concentration parties would have a dominant position with 57.3 percent of the relevant market regarding daily purchases, and with bigger purchases their share would be somewhat lower (53.5 percent). Measured by the retail space, the share of the applicants would be 69 percent; and expressed in the annual income, they would have 63.4 percent of the market. After the concentration, the Herfindahl–Hirschman Index (HHI) would be 4200 points. According to the rules applicable in the EU and USA, it is considered that there is a high concentration on a market if the HHI exceeds 1800 points, which was another reason for rejection of the request.

According to the Commission's assessment the market structure had the characteristics of an asymmetric oligopoly (Stackelberger competition) because of the different strength of the participants. The group of companies *Delta-C Market* would have the role of a leader on the relevant market, which would dictate the prices and the business operation conditions, while the other participants could only passively accept the imposed solutions (having the role of satellites).

Moreover, the Commission stated that the concentration parties were already, at the moment of the submission of the application, abusing their market power. Thus they were charging a margin that was 7 to 8 percent higher than their competitors' margin (for example, *Delta*'s margin was 18.41 percent and *Mercator*'s was 10 percent), and at the same time they enjoyed a 3-percent higher discount from the suppliers than their competitors (for example, they got a discount ranging from 10 to 25.44 percent, depending on the producer, while their competitors' got a discount ranging from 3 to 9 percent).

Primer C filed a claim with the Supreme Court again to repeal the Commission's Decision. The Supreme Court did not take the claim into consideration because of the reform of the Judicial System. Then the Administrative Court was established, which quashed the Commission's Decision in June 2011 for formal reasons (nearly four years after it had been issued).

In the meantime a new Law on Protection of Competition was adopted (Official Herald No. 51/2009). A new Commission was elected (Vesna Besarovic, one of the authors of the study ordered by *Delta* from the Faculty of Law, became its member). Immediately upon the receipt of the Administrative Court verdict, the Council of the Commission issued a new decision (hereinafter the Decision), which was finally in accordance with the desires of the concentration parties. This Decision requires a more detailed analysis.

Cooperative Decision

Before the issue of the Decision, the president of the Commission issued a Conclusion by which they linked the incompatibles – the request of *Primer C* from January 2006 for approval of the concentration created by the purchase of the *C-Market* shares, and *Delhaize*'s concentration-related application from March 2011. In the explanation of such a decision they refer to Article 117 of the Law on Administrative Procedure, which provides three requirements that must be met for a joinder of proceedings: the rights and obligations of the parties must be based on the same or similar facts; the legal basis must be the same; the authority conducting the proceeding must have the *in rem* jurisdiction. On the basis of the adopted Conclusion by the president of the Commission on the joinder of two cases, the Council of the Commission issued the Decision approving the purchase of *Delta*. Thereby *Delhaize* indirectly acquired the control over *C-Market, Pekabeta, Zvezdara* and several smaller retail trade companies. In this way *Delta*'s years-long violation of the law has been legalized.

Delta has never been given an approval to take over *C-Market*, but it has not prevented it from closing a great number of stores of this company, to change the use of the retail space (converting it into cafés, clothes shops or luxurious car salons), or from simply using these stores under its name. A vivid illustration of this trend is the continuous decrease in the number of *C-Market* stores in Belgrade: in 2007 there were 179 *C-Market* stores, and in the following years 153,

144 and 136, respectively. The *Pekabeta* and *Zvezdara* stores, which had already fallen under the control of *Delta* in a non-transparent way before the adoption of the Law, have had the same destiny. By such business policy *Delta* forced the consumers to buy provisions at its biggest stores, abusing thereby the acquired market power.

When passing the Decision, the Council of the Commission considered the case files (the *Primer C – C-Market* concentration), the application submitted by *Delhaize*, the data of the state authorities and the study ordered from the Institute of Economic Sciences. In the process the Council opted for the definition of the relevant market established by the Commission in the previous composition (and used it to pass the Decision by which the concentration was refused). It is the market that includes non-specialized stores which primarily sell foodstuffs, beverages and tobacco products (business code 52110). As such goods are sold at different types of shops and stores, which in fact are not competitors to each other (e.g. kiosks and hypermarkets), the definition of the relevant market is related to the sales at self-service stores, supermarkets, discount stores and hypermarkets (page 17 of the Decision). A narrower geographic area of the relevant market is the territory of the city of Belgrade, and the wider market is the whole Serbia. Starting from such a definition of the relevant market, it is stated in the Decision that the supply concentration is moderate. If we consider only the companies controlled by *Delta*, the HHI is 1621 points on the Belgrade market, which means that the share of *Delta* stores is just a little over 40%. If we also consider the other biggest competitors, the HHI is "approximately 1900 points". The Council of the Commission finds that such a level of concentration is acceptable.

It is striking that the Council of the Commission does not mention anywhere, even after the examination of the case files, that it is stated in the previous decision that the "HHI was over 4200 points" on the same relevant market. Accidentally or deliberately, the Council members skipped this fact. According to the EU and USA anti-monopoly practice criteria, every HHI value exceeding 1800 points is considered as a high concentration criterion. Even when the Index value is below the critical one, it can be considered that the supply concentration in one year is significantly increased if the Index value grows by more than 100 points. Consequently, the very fact that the Index was "approximately 1900 points" in 2010 is sufficiently alarming and it is a convincing argument to refuse the proposed concentration. Moreover, the Commission had at its disposal data which showed that the Index

value had grown by more than 100 points over all the previous years (between 2008 and 2009 the Index increased by 294.43 points).

The data stated in the Decision originate from the ordered study which used a different definition of the relevant market, which considers the total sales including the kiosk sales. Of course, the wider the definition of the relevant market, the lower the share of individual companies and the lower the HHI value. If we consider only the income from sales at the largest retail trade chains on the Belgrade market in 2010, then the *Delta Group* share is almost 56%, and the HHI is 3679.66 points. If we also exclude the income of the small shops and focus only on the income made at self-service stores, discount stores, supermarkets and hypermarkets, which is a narrower relevant market, then the HHI value is approximate to the one stated in the 2007 Decision, by which the proposed concentration was rejected.

Regardless of the definition of the relevant market, all the data show a high concentration of the supply on the Belgrade market in 2010. Well, which definition of the relevant market is the right one, the wider or the narrower, or should the income of entrepreneurs be included in the income on the relevant market? When searching for the right answer to this question, one should start from the situation in which consumers make their choice. A simple question should be asked – is an ice-cream seller at the Belgrade Bus Station in any way a competitor to the sales at the *Tempo* discount store in Viline Vode? If the answer is negative, according to common sense, the two sellers do not make income on the same market, in spite of the fact that the *Tempo* discount store sells ice-cream as well. The contemporary antimonopoly practice, primarily in the USA, has developed analytical methods that can precisely prove that the said answer is correct.

Unfortunately, the Regulation on the Criteria for Definition of the Relevant Market (Official Herald No. 89/09) does not mention any of the methods applied nowadays. The Regulation that was adopted on the basis of the previous Law, which was superseded by the adoption of the new Law, prescribed the application of a small, but long-term increase of the relative price test (this Regulation was confusing, because it was a poor translation from the English language, where some essential elements of the original text were missing). In any case, the applicable Regulation lacks precise criteria for defining the relevant market. However, if the Commission opted for one definition of the relevant market, it cannot use the data relating to a different, more widely defined market.

The Decision has omitted two more crucial facts which are stated in the previous Decision. The first is that the market is highly asymmetrical, that there is a leader in it, as well as a number of satellites (Stackelberg competition). Regarding this, the Decision states that this market "has marked dynamic and development characteristics" (both statements are repeated a number of times). Shortly after that, it points out how the number of shops and the sellers' income decrease, and so it is not clear on what basis it was established that the market had "dynamic and development characteristics".

The wording, according to which the market structure is changeable, does not say anything concrete. In which direction has the market structure changed? Has the market structure evolved towards Bertrand and Cournot competition? The data on the sale share on the relevant market show that in 2010 *Delta* seized more than a half of the turnover made on the relevant market, while its biggest competitors made 16, 13 and little less than 10 percent, respectively. Therefore, the market is still highly asymmetric, which is also shown by the profit rates – the return on its own capital in the years between 2008 and 2010 was between 13 and almost 18 percent with *Delta*, while the first following competitor, *Idea*, had only losses in that period. The second competitor, *Mercator*, had a loss in 2008, and in the following years its rates of return were 5.39 percent and 3.09 percent. All indicators showed the existence of an asymmetric market.

Another fact that was bypassed is the statement of the Council of the previous Commission that the *Delta Group* stores enjoyed higher margins and discounts than its competitors. This finding was simply skipped over, in spite of the fact that it had been stated in the previous Decision. No one mentioned the fact – which is not stated in the decisions of the Commission, but which is commented on widely by the public – that *Delta* has not been paying its debts to its suppliers for years. Both practices (inappropriately high margins and discounts, and non-payment for the goods sold) seriously violate the competition conditions and show a privileged position of *Delta* on the market.

Finally, at the end of this part, we have to state another fact. While preparing this Report, the Anti-Corruption Council requested the decisions from the Commission. After several requests and the engagement of the Commissioner for Information of Public Importance, the Council received a copy of the Decision in which, as in Stalinist classified documents, all the figures were deleted, including those that are available on the Internet. The data used by the Commission are of crucial significance for the issue of the Decision and they must not be

concealed from the public. The Commission is a state agency which makes decisions on the basis of the law and in the public interest, and there must not be any privileged information.

Legal consequences of the Decision

In the exposition of the Decision the Commission stated that during the procedure it received the verdict of the Constitutional Court and that, after having examined the case files and considered the case, it concluded that the requirements from Article 117, paragraph 1, of the Law on General Administrative Procedure (Official Herald No. 30/2010, hereinafter: LGAP) were fulfilled, which allowed also the possibility of the initiation and conducting of a single proceeding when the rights and obligations of a number of parties are involved. Consequently the president of the Commission adopted the Conclusion No. 6/0–02–209/2011 that allowed the initiation of the proceedings upon the application of *Delhaize the Lion* and the proceeding upon the request of *Primer C*. It is stated in the Decision that the proceeding upon the request of *Primer C* was conducted according to the 2005 Law on Protection of Competition (Official Herald No. 79/2005, hereinafter: 2005 Law), while the proceeding upon the application of *Delhaize the Lion* for examining the concentration was conducted according to the new 2009 Law on Protection of Competition (Official Herald of the Republic of Serbia No. 51/2009, hereinafter: 2009 Law), and that the application of two different laws was not an obstacle to simultaneous decision making.

According to Article 117, paragraph 1, of the LGAP, if the rights and obligations of the parties are based on the same or similar facts and on the same legal basis, and the authority conducting the proceedings regarding all the cases has the *in rem* jurisdiction, a single proceeding may be initiated and conducted also when the rights and obligations of a number of parties are involved.

In the concrete case the facts are neither the same nor similar. The subject of the request of *Primer C* was an approval to acquire the control over the company *C-Market*. The subject of the *Delhaize the Lion* application for concentration was related to the acquisition of direct control over the company *Delta Maxi* and consequently the indirect control over the companies *Pekabeta* Beograd, *C-Market* Beograd, *TP Serbia* Kragujevac, *Zvezdara* Beograd, *TP Stadel* Kragujevac and *Bell Investment Property* Beograd. The request of *Primer C* was based on the facts existing at the time of the establishment of the concentration

in 2005. The structure of the relevant market was changed following the *Primer C/C-Market* concentration. As the party that acquired the control over *Primer C* belonged to the group of companies which include also the business companies *Delta Maxi* and *Pekabeta*, the market share of *Delta* was increased by the market share of *C-Market* on the relevant retail market in non-specialized stores, which sell primarily foodstuffs, beverages and tobacco products, after the establishment of the concentration. The application for *Delhaize/Delta Maxi* concentration was based on the facts existing in 2011, which significantly differ from the facts existing in 2005. Besides the control over the company *Pekabeta* Beograd, now the company *Delta Maxi* also has control over the companies *C-Market* Beograd, *TP Serbia* Kragujevac, *Zvezdara* Beograd, *TP Stadel* Kragujevac and *Bell Investment Property* Beograd. In the period between the establishment of the two concentrations, 2005–2011, the structure of the relevant market changed also regarding the presence and the market position of other competitors, which entered the market or withdrew from it, or increased or decreased their market share in the meantime. On the other hand, the structure of the relevant market will not be changed by the institution of the *Delhaize/Delta Maxi* concentration, but rather *Delhaize* will only take over *Delta*'s market position.

The legal basis for decision making on the parties' applications is not the same either. *Primer C* submitted a request for the issue of an approval for the establishment of concentration on the basis of Article 23 of the 2005 claim. In accordance with Article 27, paragraph 5, of the 2005 Law, the Commission issued a decision by which the request for the issue of approval for the establishment of the concentration was rejected, if the requested establishment of the concentration would significantly prevent, limit or disrupt competition, primarily by the creation or strengthening of a dominant position on the market. *Delhaize the Lion* submitted an application for the examination of the concentration on the basis of Article 61 of the 2009 Law and, by the conclusion of the president of the Commission of 13 April 2011, the procedure was resumed as an *ex officio* procedure, in accordance with Article 62, paragraph 2, of the 2009 Law.

Article 19 of the 2009 Law prescribes the presumption of permissibility of a concentration. Concentrations of market participants are allowed, unless they would significantly limit, disrupt or prevent competition on the Serbian market or on a part of this market, and especially if such a limitation, disruption or prevention would not result in the creation or strengthening of a dominant position. If the Com-

mission does not issue a decision within the time limits prescribed by that Law, the concentration is considered to be approved in accordance with Article 65, Paragraph 2, of the 2009 Law. If the Commission finds that the concentration does not meet the permissibility requirements, it shall invite the applicant to declare themselves within the given period of time and to propose specific conditions they are willing to accept in order to fulfill the concentration requirements for approval. The Commission makes an assessment of the proposed conditions according to Art. 19 of the 2009 Law and issues a decision by which it approves a concentration, and sets out specific requirements and deadlines for their implementation, if it considers them eligible for the fulfillment of the conditions from Article 19.

The procedure initiated by the request of *Primer C* must be completed according to the provisions of the 2005 Law, as Article 74 of the 2009 Law provides that procedures initiated prior to the effective date of this Law are to be completed by the application of the regulations under which they were initiated. The joinder of the procedure initiated by the request of *Primer C* and the procedure upon the application of *Delhaize the Lion* has created a legally impossible situation where one procedure was simultaneously conducted under the provisions of two laws, the 2005 Law and the 2009 Law.

Finally, the competent authority was authorized by Article 117, Paragraph 1, of the LGAP to **initiate** and conduct a single procedure. The reason for conducting a single procedure was cost-effectiveness, as the competent authority in the procedure simultaneously gathered and assessed the same evidence relevant to the decision-making in several legal matters, which were based on the same or similar facts and the same legal basis. The procedure upon the request of *Primer C* was initiated on 17 January 2006 and has been going on continuously since then, as the competent court twice quashed the Commission's Decision and remitted it for reconsideration. The procedure upon the application of *Delhaize the Lion* was initiated five years later, on 9 March 2011. In the procedure initiated by the application of *Delhaize the Lion*, the Commission could not use the evidence presented to determine the facts in the procedure conducted upon the application of *Primer C* because this evidence is related to an essentially different factual situation, as it was five years ago, or four years ago, when the Commission issued its Decision in 2007. Likewise, the evidence presented in the procedure regarding the application for *Delhaize/Delta Maxi* concentration is of limited significance for the resolution of the *Primer C* request, because it is related to the relevant market structure created after the establish-

ment of the *Primer C/C-Market* concentration and upon the occurrence of other changes that followed after 2007, while the procedure regarding the request of *Primer C* determines the changes in the relevant market structure which occurred after the establishment of the *Primer C/C-Market* concentration.

Even if the requirements for the joinder of the subject procedures had been fulfilled, the Commission was obliged state its decision regarding the *Primer C* request separately in the exposition of the *Delhaize/Delta Maxi* Decision, or to issue a partial decision, which it did not do, though it was aware of its obligation to make a decision regarding the request of *Primer C*.[1] Thus it is stated in the opening statement of the *Delhaize/Delta Maxi* Decision that the Council of the Commission decided on the procedure upon the *Delhaize the Lion* application for concentration, continued *ex officio*, and on the *Primer C* request for the issue of an approval for the establishment of the concentration. However, the Decision was issued only on the basis of Article 62 of the 2009 Law, though the procedure upon the request of *Primer C* was conducted according to the 2005 Law, in the exposition of the *Delhaize/Delta Maxi* Decision the Commission "discusses" the issue of the *Primer C/C-Market* concentration as well within the scope of its decision-making on the *Delhaize* application for concentration, stating that the "Council of the Commission considered the situation in the relevant market at the time when it was deciding on the permissibility of the *Delhaize/Delta Maxi* concentration, and without considering the time when the previous (2007) Decision was made." The Commission accepted the existing situation as a fact – that the *Delta Group* had acquired the control over *C-Market* contrary to the final decision of the Commission by which the *Primer C* request was rejected, and the *Primer C/C-Market* concentration forbidden, and consequently it found "that it would not be incomplete or wrong if the market share and position of *C-Market* were treated as a market share independent of the *Delta Maxi* market share."

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[1] "The provision of Art. 198, Paragraph 1, of the LGAP prescribes that the decision on the procedure matter in whole and upon all the requests of the parties which have not been specifically decided during the procedure is specified in the disposition of a decision . ...As the challenged Decision did not decide on the request of the party, ...the respondent authority is obliged, according to Article 206 of the LGAP, to pass a supplementary decision upon the proposal of the party or *ex officio*, and decide on this request of the party which was not covered by the challenged decision." The verdict of the Supreme Court of Serbia No. U 7892/2005, dated 6 April 2006.

Obviously the Commission was not aware of, or refused to see, the serious procedural error it had made. The application of a party cannot be decided in the exposition of a decision, but only in the disposition (by Dictum), because only the disposition of a decision is legally effective (*Res judicta*).

According to the above stated, the procedure following the request for approval of the *Primer C/C-Market* concentration has not been completed yet, and the Commission has not acted according to the Administrative Court verdict, which it was obliged to do in light of Art. 61 of the Law on Administrative Procedure (Official Herald of the Republic of Serbia No. 111/2009). This is especially significant because a positive decision of the Commission in the procedure regarding the request of *Primer C*, and a decision by which the *Primer C/C-Market* concentration is approved, is a prerequisite for passing a decision by which the *Delhaize/Delta Maxi* concentration is approved. As already pointed out, the target company *Delta Maxi* controls the subsidiary company *C-Market*. If the *Primer C/C-Market* concentration is not approved by the Commission, then consequently the *Delhaize/Delta Maxi* concentration cannot be approved either because by acquiring direct control over *Delta Maxi, Delhaize* acquires also indirect control over *C-Market*. "No one can assign to someone else more rights than he has himself" says the old Latin maxim, which is applicable nowadays as well.

Analysis of the concentration effects

In assessing the effects of the *Delhaize/Delta Maxi* concentration, the Commission starts with the statement that the implementation of this concentration would not lead to the cumulation of the market shares of the undertakings, and that *Delhaize* only takes over the market position of the target company, as the concentration parties operate on the same relevant product market, but on different geographic markets (Decision p. 31). In doing so it overlooked the fact that in the same procedure it was deciding on the *Primer C/C-Market* concentration, a textbook example of a concentration with horizontal effects, where there is a cumulative market share of the concentration parties. The Commission itself states an assessment that there have been significant changes in the structure of the relevant market over the previous few years (Decision p. 33). One of the most significant changes is undoubtedly the consequence of the *Delta Group*'s acquisition of control over the company *C-Market*. The Commission had to assess first the effects

of the *Primer C/C-Market* concentration, by determining whether the concentration would prevent, restrict or distort competition, primarily by creating or strengthening a dominant position, and whether this concentration could be approved by the application of the criteria set out in Article 28 of the 2005 Law. Only then could the Commission assess the effects of the *Delhaize/Delta Maxi* concentration.

The fact is that *Delhaize* takes over the market position of the company *Delta Maxi*, but this market position has been acquired unlawfully, because the *Primer C/C-Market* concentration was prohibited by the Commission's decisions from 2006 and 2007, and it was not approved by the *Delhaize/Delta Maxi* decision.

If the argument of the takeover of a market position is accepted, it has limited validity because it takes into account only one of the criteria significant for assessing the effects of the subject concentration referred to in Article 19, Paragraph 2, of the 2009 Law – the structure of the relevant market, which remains unchanged when one of the concentration parties is not present on the relevant market. Assessment of concentration permissibility is made by applying other statutory criteria as well, all of which should contribute to reaching a conclusion about whether the subject concentration significantly restricts, distorts or prevents competition, and especially as a result of the creation or strengthening of a dominant position.

Even with an unchanged market structure, other criteria may indicate strengthening of the market position of the concentration parties and possible strengthening of the dominant position. In this regard, the following criteria are particularly important: actual and potential competitors, the economic and financial power of the concentration parties, the possibility to choose suppliers and users, legal and other barriers to entry onto a market, and the level of competitiveness of the concentration parties. The Commission did not assess these criteria, although it had at its disposal the data on the competitors' presence on the Serbian market, on the economic and financial power of the concentration parties, and the legal and other barriers to the market entry. Some of these data are stated in the exposition of the Decision, but the Commission does not give their assessment or just makes sweeping generalizations (such as that "there are no alarming signals that indicate the existence of entry barriers for access to this market").

Application of the said criteria should lead to an overall assessment by the Commission which would give an answer to the following question: will there be, after the implementation of the concentration,

an increase in prices of goods offered by the concentration parties, will the concentration be harmful to the interests of consumers? Such an assessment is missing.

Sale conditions

The Anti-Corruption Council did not see the Sales Contract, and the elements of this Contract, which were included in the Decision, are hidden from the public by the decision of the Commission. Thus we have no answers to many questions of public interest. At the moment we only have the information stated at press conferences by the very parties to the agreement.

The sales price was established on the basis of the economic value (EV) of the company. This term is used in situations where it is not possible to objectively assess the value of the capital. When it comes to countries that do not have a developed capital market, or when an the object of sale is a company whose shares are not listed on the stock market and, at the same time, the accounting data are not very reliable, a subjective assessment of the EV is made.

In order to obtain the EV of a company, we start from the estimated value of the sales in the current year and that amount is multiplied by a coefficient chosen subjectively. Of course, this coefficient cannot be determined quite arbitrarily, but rather it depends on the characteristics of the entire industry, and on the fact of whether it expects a dynamic growth or stagnation, if the whole economy is progressing, or if a reversal in the perceived trend may be expected, etc.

So, there are several factors that experts have in mind when trying to determine the EV. The coefficient usually ranges from 3 to 4, and even to 17 with propulsive industries. Simply put, the EV should show the company's ability to generate revenue in the future. The company's debts must be deducted from the obtained EV in order to obtain a price suitable for a buyer.

The buyers started from the assumption that this year *Delta*'s revenue would be about one and a half billion. They multiplied this amount by the coefficient of 0.67 and thus obtained an amount of 932.5 million euros. At a press conference in Brussels the buyers stressed that *Delta* was bought cheaply because the coefficient of 0.67 is lower than the one recorded in similar transactions, lower even than the ones characterizing the region of Southeast Europe (0.84). If this ratio had been applied, the EV of *Delta* would have been 1.26 billion euros.

Of course, the company's debts must be deducted from the EV amount in order to obtain the price that is paid to the seller. For the time being the parties have not disclosed this price publicly, but have only pointed out that the EV includes "the costs of adjustment and debts amounting to approximately 318 million euros". As debts, they have pointed out especially those owed to banks. We do not know what part of the amount of 318 million euros accounts for debts to banks, to suppliers, and how much the costs of adjustment are.

The press has speculated on the fact that the debts of *Delta Holding* exceed 900 million euros. However, again, it has not indicated what the debt of the retail chain within the Holding Company is, or how much is owed to suppliers. From the macroeconomic point of view, debts to suppliers have priority because, if a company has sold its goods through *Delta* and is unable to collect the receivables, it becomes insolvent. In other words, the company is forced to take bank loans with very high interest rates, which leads to losses, and, when liabilities exceed possible income, the company is forced to bankruptcy.

Probably many of *Delta*'s creditors have been made happy by the news of the sale of the company to the retail giant, whose annual revenues exceed 20 billion euros, and whose net profit amounted to 574 million euros in the last year. However, the manner in which the sale has been carried out does not give cause for great optimism.

Delhaize is a group of a number of companies, which, as a rule, are not liable for the obligations of the group members. Every shareholding company or limited liability company is liable for its obligations only up to the amount of its initial capital. One of the members of the *Delhaize Group* is the Dutch holding company *Delhaize the Lion*. On 30 January this year it established a holding company *Lion Retail Holding*, based in Luxembourg, in order to buy *Delta*. The decision only states that the Luxembourg company has never had any business activities and it does not specify the amount of its initial capital. The assumption is that, for now, only the minimum amount has been invested, which is, according to Luxembourg regulations, required for the registration of a company. In other words, creditors, whose debts will eventually be recognized in a court proceeding, will not probably be able to collect the same from *Delhaize*. In the end, these debts will have to be paid by local taxpayers.

Another important enigma of the sale refers to the potential tax revenue for our country. These revenues are uncertain due to the fact that both the buyer and seller are registered abroad. The buyer is reg-

istered in Luxembourg, and the seller in Cyprus. The owner of the Cyprus company is a Virgin Islands phantom company whose ultimate owner is concealed. In such a situation it is not clear who is obliged to pay tax on the transfer of absolute rights. Tax on capital gains should make a substantial amount of tax revenue. There is no doubt that *Delta* acquired the shares of *C-Market, Pekabete, Zvezdara, Si Market* and several smaller companies at a lower price and has sold them at a higher price. The difference is the capital gain. According to the Income Tax Law, capital gains tax is charged at a rate of 10%.

Considering the fact that *Delta* has been sold as a whole, the question is which part of the sale price relates to the purchase of these subsidiaries. A possible answer could be obtained starting from the size of the retail space. Specifically, *Delta* used the entire retail space of its subsidiaries and that space can still be used for the core business activity. According to the official data, in 2010 the space of *Delta*'s subsidiaries accounted for more than one third of its business space. However, one should bear in mind that *Delta* has simply renamed some stores of its subsidiaries into its own stores. Thus, for example, between 2007 and 2010 the *C-Market* retail area was reduced by as much as 8,519 square meters (one sixth). Consequently, the share of the retail space belonging to the subsidiaries is certainly higher than stated in the request for concentration.

Possible courses of action by the Government

The number of options that are available to the Government is significantly reduced after the sale of *Delta* to *Delhaize*. The retail trade monopoly created in Belgrade by the acquisition of *C-Market* by *Delta* can no longer be eliminated by the return to status quo ante. By its decision the Commission has legalized the monopoly created by force, ignoring at the same time years-long abuses made by the monopoly holder using their dominant market position. In such a situation the only thing left for the Government is to try is to strengthen the competition by attracting retail chains which are already active in the region. In this way the market share of the dominant company would be reduced and the space for possible abuses would be narrowed.

Attracting new competitors will certainly not be easy in times of an economic crisis. Investors still refrain from investing and turn primarily to emerging markets. Our market is in regression and the retail

trade sales have been declining for years. This trend is likely to continue as unemployment is rising and the purchasing power is declining.

Besides, foreign investors have in mind the negative experiences which some of the largest firms had in Serbia. Thus, when trying to buy the shares of the Serbian largest producer of mineral water, *Danone*, one of the most famous food and drink producers, was forced, by manipulations of Serbian tycoons and politicians, to quit the race. *Brief* trading company, which legally acquired land for construction of a large shopping center in Belgrade, had an even worse experience, as it was exposed to tremendous bureaucratic obstacles, because the owners of the *Port of Belgrade* /*Luka Beograd* / wanted that land. In the end *Brief* decided not to make the investment and thus an opportunity to have the level of competition on the Belgrade market increased was irretrievably missed.

The Government must ensure the security of property rights, not only of foreign but also of domestic investors. Application of regulations must not be personalized – the same rules must apply to all. Long-term delay in payments to suppliers must not be tolerated to some, while others are forced to bankruptcy for the same reasons. The fact is that some individuals secure a privileged position for their companies owing to their connections with political leaders. Undoing these connections is certainly a prerequisite for functioning of the rule of law, without which there is no protection of property rights, which is indispensable in order to attract investors. This requirement is probably beyond the capabilities and ambitions of the present government and, therefore, we shall recommend here below how these not-so-unattainable goals can be achieved.

Cutting the Cyprus Network

In the last decade of the last century undetermined amounts of money were taken from Serbia to Cyprus. It was during the blockade of commercial and financial links due to the UN sanctions. The money was carried by couriers to the Cyprus branch office of the ***Belgrade Bank /Beogradska banka/*** (BB COBU), and then it disappeared without a trace in the network of phantom companies that were established by persons trusted by the government. After the change of the regime in 2000, a political delegation was sent to Cyprus and, only after a few days, it concluded that "there is no money" there. Such a conclusion was at least politically irresponsible and professionally unacceptable.

However, since then all relevant institutions in the country have acted as if it were an insignificant, established fact.

As money cannot magically disappear, but rather has to be spent on something, the Hague Tribunal was interested in whether a part of the funds had been used for procurement of military equipment. Norwegian expert Morten Torkildsen was engaged for this purpose, and he found out that the assumption of the Prosecution was justified. He found out that the phantom companies controlled by Serbian citizens used the money that had been taken out of the country. From a very limited sample, he found out that more than a billion dollars had been spent on purchase of military equipment. The Court was not interested in establishing how much money had been taken out of the country in total, or how much of it was spent on other items. However, it has been proved that the money can be traced and that the persons who controlled the cash flows can be revealed.

Torkildsen has found out that these companies, in the translation called "front companies", were established not only in Cyprus but also in Greece, Germany, Austria, Switzerland, Luxembourg, Liechtenstein, Singapore, Monaco, Guernsey, the Isle of Man and Jersey. In European countries he could trace cash flows and discover the true owners of the companies without any particular problems. Problems were encountered at the so-called tax havens where they register companies that conceal the owners. Their interests are most frequently represented by law firms, which are not obliged to reveal the names of the owners or make their financial statements available. However, things are improving there as well, and tax havens are no longer so opaque.

The UN Convention Against Corruption (Merida Declaration) has been adopted in which all signatory states undertake to cooperate in the discovery of illegally acquired assets. The World Bank has also launched an initiative to restore the stolen property. The aim of the Initiative is to provide technical assistance to countries to trace property taken out of a country illegally during a period of dictatorship. The key document of the Initiative, published this year, deals with detection of hidden owners of legally established business companies (*The Puppet Masters*). Besides, in recent years many countries have adopted, within the fight against terrorism, their own regulations, which have, to a large extent, intensified the control of cash flows. Thereby, they followed the recommendations of the Intergovernmental Working Group for Prevention of Money Laundering (*The FATF 40 Recommendations on Money Laundering*).

The Government should use all the possibilities offered by international norms and institutions created to control cash flows, in order to finally determine how much money has been taken out of the country, how much of it has been spent on what, through whose companies the funds were directed and under what conditions. Only then will it be determined whether and how much money is left in the accounts abroad, who has been using this money, and how, and whether it is perhaps being returned to Serbia in the form of "foreign investments".

For this purpose it is necessary to establish an inter-ministerial commission, which would be composed of experts from the Ministry of Finance, the Ministry of Internal Affairs, the National Bank, the Agency for Rehabilitation and Bankruptcy of Banks, and the Privatization Agency. The Commission must consist of experts and its work must not be restricted by political pressures, as it has been so far. It must have access to all information available in Serbia, particularly the archives of the security services, which controlled the work of the trusted persons – founders of the phantom companies. The results of the Commission's work must be disclosed to the general public. Simultaneously with the professional investigation, which would lead to the opening of court proceedings, it is necessary to initiate a political investigation. The Government should initiate the creation of a parliamentary committee, which would include representatives of all parties. Its task would be to examine the political and economic consequences of the "Cyprus Connection" and to suggest a possible amendment and improvement of the law.

Revealing true owners of companies

In many cases where the Council has done research, foreign companies whose owners, business, and equity capital were unknown, or which had no operating income, have been involved in possible corruption. Usually, the interests of these companies were represented by law firms which concealed their true owners, and even when they were ready to disclose them, it turned out they were owned by some other companies registered in even more exotic places. The so-called off-shore legal regimes used different solutions in order to effectively conceal the true owners. In some cases it is impossible to discover the owners, same as in cases where bearer shares are issued (the owner's name is not entered in the register).

We had also a similar situation when a monopoly was created on the Belgrade market. The *C-Market* shares of individual employees

were bought off by *Primer C*, which had neither any equity capital nor any operating revenues. The ownership of *Primer C* was transferred to a Luxembourg company controlled by Milan Beko. During his testimony in court he could not even remember the name of the company and explained that it was a shell company. It turned out that the Luxembourg company was owned by *Hemslade* from Cyprus, and this one was 100% owned by *Hitomi* from the British Virgin Islands. The Commission for Protection of Competition did not want to find out who owned the company *Hitomi* and there the story came to an end.

The Anti-Corruption Council considers that the use of phantom companies is the main channel through which large-scale corruption operates. Therefore, it is necessary to prevent the operation of business companies whose owners are not known. During the registration of companies, the names of natural persons who are the ultimate owners of such companies must be presented. The ownership chain must end with a natural person. S/he may be the ultimate owner, or the person who enjoys the benefits of the ownership (because an ultimate owner cannot be a false owner who exercises the property rights in the interest of another person). All business companies must be obliged to immediately register all changes of the controlling owners. To achieve this, first it is necessary to amend the regulations relating to the operation of the Business Registers Agency, the Securities Commission and the Commission for Protection of Competition.

In accordance with the recommendations of the FATF, OECD and the World Bank, the obligation of revealing the true owners should not only be an obligation of public authorities, but of all financial institutions, consulting companies and law firms (service providers). Perhaps these tasks are too ambitious for the coalition government which is at the end of its term of office. Therefore, we shall speak about more modest and easily achievable goals.

Defining the relevant market

At the time when amendments to the 2005 Law on Protection of Competition were prepared, the Anti-Corruption Council urged, in its several letters to the Government, the importance of accurately defining the relevant market. Without a precise definition of the relevant market, it is impossible to determine the dominant position of undertakings on a market. Specifically, if a market is broadly defined, the share of each producer is smaller and, consequently, the HHI value, as a measure of market concentration, is lower.

The Council pointed to the weaknesses of the legal definition of the relevant market and to the unintelligible text of the government regulation that was adopted for the purpose of defining the procedure for determining the relevant market. All these letters were simply ignored, and the new Law (Official Herald No. 51/09) in Article 6 introduced only some stylistic changes in comparison with the same article of the previous law. To make matters worse, the Regulation on the Criteria for Defining the Relevant Market (Official Herald No. 89/09) was adopted on the basis of the same article, which is even less precise than the previous regulation.

Bad consequences came to the fore very quickly, in fact already with the first decision taken by the new Commission. The Decision only stated what the relevant market was in the concrete case – the sale in general stores selling mainly food, beverages and tobacco in self-service shops, supermarkets, discount stores and hypermarkets, thereby giving no explanation, nor specifying the methodology applied. Then the results of the ordered study, which used the broadly defined relevant market – total sales in non-specialized stores selling primarily food, beverages and tobacco (Business Code 52110) – are stated in the Decision. Accidentally or intentionally, the members of the Council of the Commission used the results which show a lower *Delta* share than the actual one.

Such imprecision must not be tolerated. One must not, on the basis of the same data, state first that a company has a dominant position, and then that it does not have it. Therefore, it would be best to include in the Law itself the provisions on the methodology used in defining the relevant market. However, as it is a process that requires the knowledge of a more complex economic analysis, the easiest solution may be that the Law refers to the procedure applicable in the EU (OJ S 372 of 9.12. 1997).

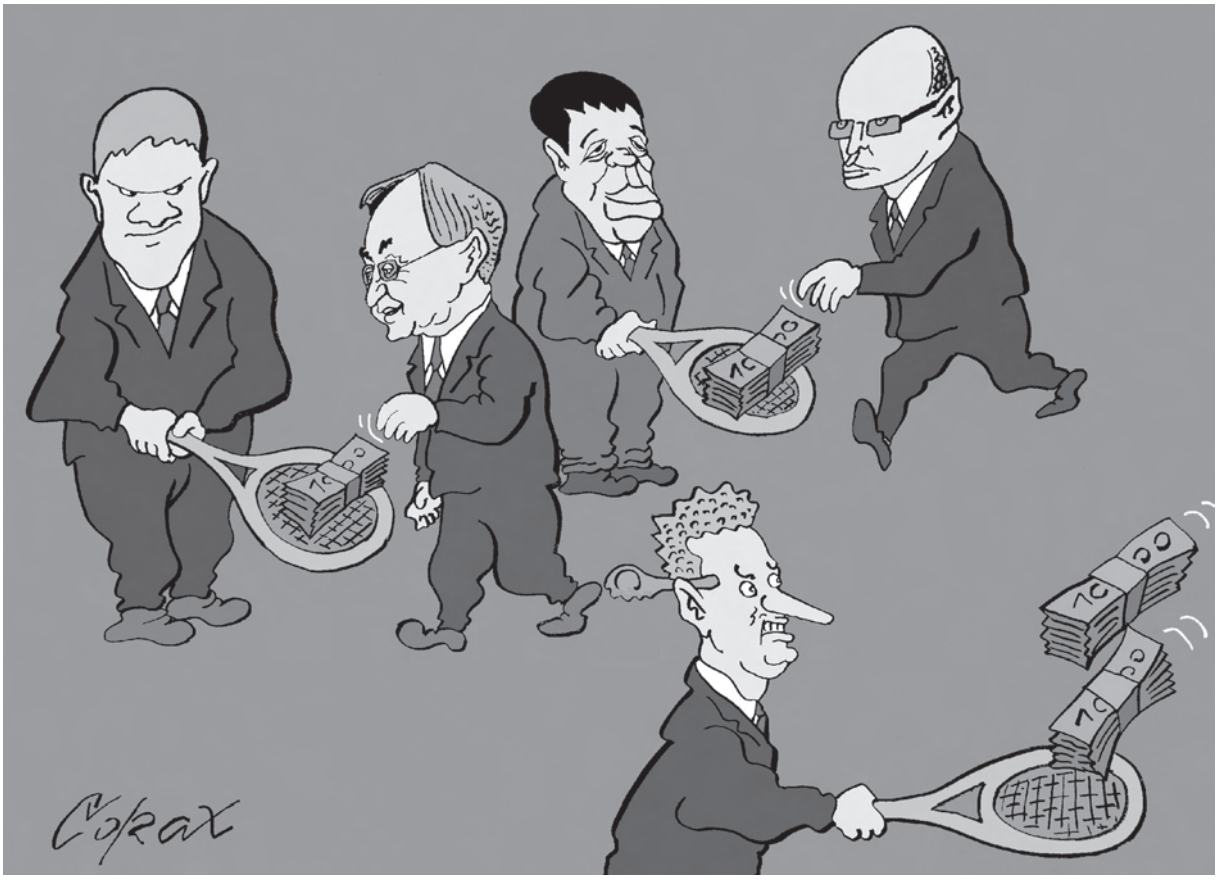
Conflict of interest

The current provisions on the incompatibility of offices and jobs, and on conflict of interest (Articles 27 and 28 of the Law) should be specified more precisely and amended. A person who publicly defends the interests of monopoly holders must be neither nominated nor elected as a member of an independent regulatory body that regulates the operation of monopolies. If we allow such a conflict of interest, the fight against monopolies and their detrimental impact will become illusory.

Unfortunately, this is not an isolated case. For example, the lawyer who defended the interests of the *Port of Belgrade* /*Luka Beograd*/ in the aforementioned dispute with the trade company *Brief*, was elected to the body that manages the construction land in Belgrade. Should we recall that the owners of the *Port of Belgrade* were at the same time the owners of *Delta.* This certainly confirms the fact that tycoons have a privileged position in our political and economic systems. Such privileges always go hand in hand with large-scale corruption.

If the Government undertakes any of the recommendations, it will make the first significant step in the fight against large-scale corruption. The Anti-Corruption Council does not lose hope that this step will be taken, in spite of the fact that our experience with the Council reports so far has been discouraging.

Yours faithfully,
President
Mrs. Verica Barać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САВЕТ ЗА БОРБУ ПРОТИВ КОРУПЦИЈЕ
ВЛАДЕ РЕПУБЛИКЕ СРБИЈЕ

КОРУПЦИЈА, ВЛАСТ, ДРЖАВА

III ДЕО

Приредила
Верица Бараћ

Београд
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