

# Public interest in the mud, smoke and under the water

Case studies of three big projects in Serbia

Public procurement, public private partnership and state aid projects in Serbia –  
national and European rules vs. international agreements

Transparency Serbia  
2016.



Transparentnost Srbija  
Transparency Serbia

# Public interest in the mud, smoke and under the water

Case studies of three big projects in Serbia

Public procurement, public private partnership and state aid projects in Serbia –  
national and European rules vs. international agreements

Transparency Serbia  
2016.



# Contents

<b>Background</b> .....	04
Summary of main findings and conclusions.....	06
Interstate agreements and anti-corruption rules in Serbia - Constitutional aspect.....	14
Stabilisation and Association Agreement.....	19
<b>Smoke</b> .....	33
The review of the agreements between the Republic of Serbia and the People's Republic of China and the reasons for their adoption.....	33
Previous agreements.....	35
Agreements with China, the application of the laws of the Republic of Serbia, the economic and other effects.....	38
<b>Mud</b> .....	45
Public procurement experiences - pumping water and silt from the open pit.....	45
<b>Water</b> .....	53
Belgrade Waterfront - (media) genesis of the case.....	53

## Background

Republic of Serbia is country in South-East Europe. Since 2001, Serbia's aspiration is to become member of EU. In 2008 Serbia signed Stabilisation and Association Agreement with EU that came into force on September 1<sup>st</sup>, 2013. EU and Serbia formally launched negotiation process in 2014 and opened first chapters in 2015.

Like its neighbouring countries, Serbia has problems with corruption in its public sector. This problem is tackled through numerous laws and policies. Prioritization of fight against corruption on national and EU agenda resulted in development of rules and procedures in the areas such are public procurements, public-private partnerships and state aid. By the rule, laws are calling for open market competition, transparency, analyses of effects, grievance procedures and other channels for protection of public interest.

Huge infrastructure projects bring serious risk of corruption, worldwide. It is not only about amount of potential illicit gain, but also about possibilities to hide misconduct or cost of the project. Infrastructure projects are also loved by politicians. Once implemented, such projects are ideal for political promotion, as they may impress potential voters. There are also some economic benefits of such projects, such as increase of employment and GDP. While benefits are visible, costs stay often hidden.

Infrastructure projects are, by the rule, financed through the banks' or foreign countries' loans, due to lack of state budget funds. It also affects legal procedures, since loan-givers insist on special provisions that are accepted by the loan – taker. The situation becomes more complicated when such special provisions are based on interstate agreements, thus being superior to national legislation.

European integration also brings an issue of super-national character of EU rules. However, at least before the accession and in the field of anti-corruption, these rules are not detailed enough, but rather set as broad standards and may be interpreted in various ways. However, it is clear that EU rules favour competition, open market and transparency of public finances. In that ways, these rules may potentially protect from direct contracting hazards.

Transparency Serbia, as non-governmental organization and branch of Transparency International is active in the field of public procurement since 2002. More recently, we start dealing with other types of public contracting such are public – private partnerships and various forms of state aid. Transparency Serbia is monitoring implementation of rules and formulation of policies, but also advocate for changes, suggest amendments to the legislation and educate the public about these issues.

We recognized risks from implementation of direct negotiation long time ago and proposed several measures for their mitigation. Among other things, Transparency Serbia suggested this issue to be properly tackled through National Anti-corruption Strategy, adopted in 2013. However, provisions related to the inter-state agreements that circumvent national legislation were removed from the first draft, without explanation.

Likewise, Transparency Serbia recognizes opportunities of EU integration to suppress corruption and build up more effective system of legal rules. Such rules may be originally imposed in order to protect interests of EU firms. Once the market competition becomes the rule it also protects citizens' interests, by providing them better "value for money" in infrastructure projects. However, we are aware of limits of EU mechanisms, being either consequence of underdevelopment of the legal system or the prevalence of political considerations.

Besides the issue of formal compliance with the rules, the matter of our monitoring is also issue of public interest protection. Namely, before the decision is made to enter certain legal procedure, not to say contract, there should be some cost and benefit analyses. Ideally, such analyses should be made public. Interested parties, experts and other citizens should be invited to provide their input in formulation of the policy. In order to make such discussion effective, analyses should present not just immediate benefits of one solution, but also its longer terms costs. Furthermore, such benefits should be compared not just against the situation where there is no project at all, but also with its potential alternatives.

This analysis explains how the system functioned in three case studies where the public contracting took place during 2014 and 2015. Besides that, the analysis presents general discussion about inter-state agreements and potential benefits of SAA in observed areas. We used findings of draft analyses in public debates and advocacy activities during this project and had also some success in legal reforms and public awareness raising, but also interest of stakeholders.

## Summary of main findings and conclusions

This study deals with public procurement, public private partnership and state aid projects in Serbia. National and European laws and practice in Serbia are examined through three case studies of large value projects. Special emphasis is made on international agreements as a tool to evade anti-corruption mechanisms in domestic laws.

The analysis explains how the system functioned in three case studies where the public contracting took place during 2014 and 2015. Besides that, the analysis presents general discussion about inter-state agreements and potential benefits of Stabilization and Association Agreement in observed areas.

Attention is also paid to Constitutional provisions regarding international legal acts and practice, set by decisions of the Constitutional Court of the Republic of Serbia. Namely, Constitutional provisions provide that the agreement with a foreign state regulates the relations between the parties in a different manner than it would be the case with the application of national legislation (law) only if it is not contrary to other norms of the Constitution itself. As for practice, there have only been a dozen cases where the constitutionality of the provisions of an international agreement was disputed and all these initiatives were rejected.

This analysis explained in details one of those cases, particularly interesting, the decision on the rejection of the initiative that challenged the constitutionality of some provisions of the so-called “oil-gas agreement” between the Republic of Serbia and the Russian Federation, which gave dominant position to the Russian side in the biggest Serbian oil company under rather favourable conditions.

The analysis about this case concluded that there were no constitutional provisions that would limit the will of the Parliament. If the implementation of direct negotiation, dealing with public assets, cannot be challenged, and if it is not possible to legally oppose decisions of the parliament and government for their damageable economic effects, it means that Constitution does not protect from such damages no matter how big they are. Theoretically, the Parliament may agree to sell for 1 USD only all public property or to take 1000 Billion USD loan under whatever conditions. If being part of inter-state agreement, such a decision would be considered in accordance with the Constitution.

The report also analysed obligations of Serbia in relation to Stabilization and Association Agreement. The norms of international agreements that Serbia has so far concluded with third countries are not contrary to those parts of the SAA which stipulate explicit obligations or restrictions for Serbia. The only exception may represent some actions which are, on the basis

of bilateral agreements, providing state aid to enterprises. In this respect, one of violations of the SAA was also ascertained in the Progress Report for Serbia for 2014 – that the report on granted state aid has not be delivered. However, with regards to certain areas, such as energy or foreign investments, where in the SAA, instead of prohibitions and obligations, principles of cooperation were determined, the situation may arise in which treatment of Serbia could be assessed as incompatible with objectives which are underlying the SAA conclusion.

As for infrastructural object in general, the report pointed out that huge infrastructure projects bring serious risk of corruption, but they are loved by politicians. Once implemented, such projects are ideal for political promotion, as they may impress potential voters. There are also some economic benefits of such projects, such as increase of employment and GDP. While benefits are visible, costs stay often hidden.

Infrastructure projects are, by the rule, financed through the banks' or foreign countries' loans, due to lack of state budget funds. It also affects legal procedures, since loan-givers insist on special provisions that are accepted by the loan – taker. The situation becomes more complicated when such special provisions are based on interstate agreements, thus being superior to national legislation.

European integration also brings an issue of super-national character of EU rules. However, at least before the accession and in the field of anti-corruption, these rules are not detailed enough, but rather set as broad standards and may be interpreted in various ways. However, it is clear that EU rules favour competition, open market and transparency of public finances. In that ways, these rules may potentially protect from direct contracting hazards.

Theoretically, before the decision is made to enter certain legal procedure, not to say contract, there should be some cost and benefit analyses. Analyses should present not just immediate benefits of one solution, but also its longer terms costs. Furthermore, such benefits should be compared not just against the situation where there is no project at all, but also with its potential alternatives. Such analyses should be made public.

On of the three concrete cases studied in the report was construction of block B thermal power plant in Kostolac, based on the 2009 agreement between the Republic of Serbia and the People's Republic of China.

The law, adopted on 2015, confirmed the loan agreement for the privileged buyer's credit for the second phase of the project package "Kostolac B Power Plant Project". The first phase included revitalization of two existing blocks B1 and B2, of 350 MW each, desulphurization project for two existing blocks, and the second phase construction of new block B3. The approximate price for

the implementation of the whole Project Package was agreed in the amount of \$ 1,060,230,000, of which \$ 344,630,000 related to the value of the first phase, and \$ 715,600,000 to the value of the second phase.

The report pointed out that General Agreement on economic and technical cooperation in the field of infrastructure between the Government of the Republic of Serbia and the Government of the People's Republic of China, from 2009, with amendments from 2013, in the preamble stated, among other things, that the goal was "improving cooperation ... **in accordance with their national legislation and the provisions of this Agreement.**" In other words, the Agreement should be interpreted in such a way that a deviation from the national legislation is seen as an exception instead of a goal, and which is possible on the basis of the agreement.

Article 5 of the basic Agreement, however, governs the exemptions from the application of Public Procurement Law and the Law on PPP. This is achieved by anticipating that the relevant Chinese trade associations **can suggest qualified contractors for participation in projects**, and that a list of recommended contractors for each project is submitted to the country which implements the project.

Article 5 does not exclude the automatic application of the entire Law on Public Procurement, but exempts its key provisions, stipulating that "agreements, contracts, programs and projects prepared in accordance with this Agreement on the territory of the Republic of Serbia **are not subject to the announcement of a public tender for performing investment projects and delivery of goods and services, unless otherwise specified by a commercial contract.** Therefore, competition may be applied, but only if it is planned by a specific agreement. Besides the non-application of Public Procurement Law of the Republic of Serbia, these provisions exclude the obligation of tenders on some other basis and in some other ways (e.g. by the application of Chinese regulation or some other procedure). However, Article 7 of the Serbian Law on Public Procurement also indicates that this Law is not applied when procurement is implemented on the basis of an interstate agreement.

It is interesting that one of the listed arguments for the conclusion of this agreement is the "big deficit of Serbia in trade with China." It remains unclear in what way could these deficits be reduced by bringing Chinese investments to Serbia according to the adopted model, since this model involves the procurement of goods from China, paying the Chinese companies to carry out the works and the like.

Both the basic agreement and the two Annexes were proposed for ratification stating that they do not create obligations for the budget of the Republic of Serbia. This assertion is fundamentally incorrect, especially for Annex 2, which stipulates the exemption from VAT and customs duties

and which necessarily reflects in the future budget revenues. The explanations of these draft laws also lacked a mandatory part - the statement of compliance with European Union regulations.

The explanation of the loan agreement for the second phase of the project in Kostolac claimed that the agreements were economically feasible. However, such a conclusion couldn't be drawn unambiguously on the basis of the published documents. The explanatory note did not specify what would be the direct financial benefit from the realization of the project and the extent to which it would exceed the value of the approved loan with interest and additional benefits. In order for the analysis of the loan cost-effectiveness to actually be carried out, other parameters are also required, and these parameters remained unknown in the explanation of this law.

If we accepted as highly probable assumption that Serbia received a loan on favorable terms, (in regards to the interest rate and repayment period), the question remains whether these positive effects are being overrode by other contractual obligations? The agreement anticipates the engagement of companies from the creditor's country, which eliminates possible competition that could perhaps result in a more economically advantageous final tender. The agreement also stipulates that "goods, technology and services to be procured from the loan funds will be purchased mainly from China, according to the commercial contract".

In addition, the agreement anticipates the exemption from VAT and customs duties on imported equipment, which also carries a negative impact on public revenues that should be subject to consideration when determining the economic viability of the contract.

Another aspect of economic observation of the loan agreement refers to alternative solutions to the subject of procurement – e.g. how much it would cost to invest in other energy sources that could provide the same level of energy stability of the country, employment and the like. Also, one should take into account the responsibilities that Serbia assumed in connection with the important introduction of energy sources that carry less pollution, and which are not achieved by this investment. On the contrary, even further investments would be needed for "alternative sources" of energy because the volume of production of electricity from coal power plants would increase.

In order to find out more about arguments that Serbian parliament, government and EPS had in mind when accepting this legal arrangement Transparency Serbia asked Serbian authorities for additional documents. Basis for the request was the claim of the Government from the explanatory not of loan ratification law: ***the financial analysis performed on the basis of cost-effectiveness Study showed that the implementation of the second phase is economically viable and cost-effective.***

However, the only document identified by relevant ministries and public enterprises was “The bankable feasibility study on construction of the new unit rated 350 mw at the location of thermal power plant Kostolac B”. This study was prepared by the ME Energoprojekt in December 2013 for the EPS. This document is examined thoroughly in this report. The report concluded that the most crucial question remained unanswered. **Neither offer of Chinese company nor loan conditions were compared against alternative solutions of building and financing of the same Plant in other way.** So, even if this feasibility study was discussed in the Parliament along with the whole contract, neither MPs, nor citizens would know anything more about cost-effectiveness of this investment model.

The second case is public procurement for pumping water and silt from the open pit, flooded in 2014 floods. The PE Kolubara surface coal mines were flooded with millions of square meters of the water and mud. The PE Kolubara used its own equipment to remove the water, but it was not enough. Public procurement took place and works on pumping the water and silt took place few months later. The information about financing of that project was controversial, in particular in terms of World Bank's role. While the procedure of public procurement was the one from the Serbian law, some government's official claimed that tender was organized as the World Bank insisted on it.

The case of "Kolubara", presented in details in the report, revealed some possible shortcomings in the system of public procurement, which could be responded to by means of legislative intervention.

Namely, in this case the Purchaser suffered damage which exceeds the value of the actual public procurement that was conducted for the purpose of the damage elimination. According to some estimates from the EPS (that are probably overestimated), the damage amounted to around one million euros per day, and the total value of the work that was contracted with external partners was about 15 million euros. If these estimates are accurate, 15 days for the implementation of procurement procedures would cost as much as the entire acquisition. Even if in a particular case the estimate is not accurate or comprehensive, it is obvious that such a case could occur in conjunction with another acquisition.

Therefore, from the standpoint of cost-effective handling of public resources, which is one of the principles of the Law on Public Procurement, there are the reasons to procure as soon as possible, even in situations where this may result in paying slightly higher price to the supplier. It is important to note that such situations may also occur when purchases are not caused by damage from natural disasters, but by some other reasons, for example, when it is known that the price of some goods would significantly increase during the time needed to prepare and implement public procurement procedure. However, the Public Procurement Law contains **no provision**

**that the Purchaser who wishes to make the best use of public resources could refer to.** Of course, with the possible implementation of such exception, the legislators would have to act cautiously in order to reduce abuse to the minimum possible extent.

Another potential solution and formulation for specific norm, presented by Transparency Serbia in early 2015, are also explained in the study. Some of those proposals, as stated in the analysis, inspired changes to the legislation, adopted in August 2015.

The third case elaborated in the analysis is the ambitious expansion plan "Belgrade Waterfront", the project (as originally announced) worth about 3 billion Euros. Transparency Serbia analysed question of law application, transparency, handling of public resources in areas related to public-private partnerships and potential corruption risks. The project was first introduced as part of Aleksandar Vucic 2012 campaign for Belgrade City Mayor. At the time, he claimed that project would cost 125 million Euros for municipal development, but that **"the city should keep 451 million euros from the taxes for building land."** He also claimed that there were scores of investors interested in participation in the project. It ended without public competition, with one investor, not paying taxes for building land, investing 150 Million USD instead of 3 Billion Euros. It was all based on Cooperation Agreement between the Government of the Republic of Serbia and the Government of the United Arab Emirates. Therefore, anti-corruption provisions, tools and mechanisms from the Law on PPP were not used, there was no study which should explain the choice of PPP instead of some other form of project realization, there was no **cost assessment and analysis of obtained value compared to the invested funds**, there was no specifications of financial admissibility of PPP for a public body, **specifications in terms of project funding** and the availability of funds, **the planned allocation of risk**, followed by the **analysis of economic efficiency of the proposed project**, the types and amounts of collateral provided by the partners in the project, and the mechanisms for monitoring the realization of the contract and the commitments, which includes (according to Law on PPP) the regular, six-month reporting.

The analysis explains in details all steps in this case, from Vucic's 2012 campaign, through changing of the laws and strategic documents to comply with investors wishes, to signing of the contract and 5-months fight for publishing the contract.

## **Recommendations:**

Bearing in mind the legal framework, the practice (especially presented cases), the reached level in the fight against corruption, corruption risks, as well as the current Anti-corruption strategy, Transparency Serbia recommends:

### **1. The introduction of constitutional restrictions for undertaking financial commitments:**

In Serbian legislation there are some restrictions on the disposal of public assets and undertaking obligations, both in terms of the amount of commitments, and in terms of procedures that must precede the conclusion of the contract (for example, limit of public debt in the Law on the Budget System, the public procurement rules, the rules on public - private partnerships and concessions). However, these restrictions are directly violated by some laws (e.g. laws authorizing loans and issuing guarantees for loans, international agreements that allow contracting procurement, sales of public assets or forming a joint venture with a predetermined company or partner from a predetermined country). The absence of constitutional limitation makes it impossible to successfully challenge such acts which may lead to disproportionate obligations for future generations and to the renunciation of valuable public assets, for the sake of short-term benefits.

## **2. Anti-corruption mechanisms in the national laws (such as Law on PP, Law on PPP) should be used even when contracts or investments are based on international agreements.**

Conclusion of a public-private partnership (PPP) on the basis of international agreements, without the application of the PPP Law, without competition and without any obligations imposed by monitoring and reporting is one of the biggest obstacles to the establishment of formal or less transparent system of PPP. Intergovernmental agreements allow not applying anti-corruption mechanisms by domestic law. But they do not forbid it. With projects of great political interest for the government, it is the question whether we can match the economic interest of the state and political interests of the ruling party.

Therefore, in the field of PPP, it is necessary to:

1. Apply anti-corruption mechanisms in the Law on PPP, even in cases where the permitted exceptions to the application of the law (e.g. international agreements);
2. Amend the Law, in order that feasibility study for entering the PPP was required for all forms of PPP and to establish a mechanism for control of fulfilling this obligation;
3. Change of legal status and responsibilities of the Commission for PPP (extension of authorization, including monitoring the fulfilment of the obligations of the private partner, professionalization of management and professional services, etc.).

## **3. Performing and publishing analysis of financial benefits of loans received as part of international package (loan+ investment+ hiring specific contractors)**

When the Serbian Parliament ratified the Chinese loan for "Kostolac", it also agreed that the work would be carried out by company from the People's Republic of China. In the explanation of the Act that came into the Assembly, it said there had been done the cost-benefit analysis, which

allegedly proved that this arrangement ("loan - public procurement of contractor from China solely") was favourable for Serbian side. Transparency Serbia has asked the Ministry of Finance (which has prepared a draft law on Ratification of the loan) for a copy of the analysis. They informed us that they didn't have it, and we were directed to the Ministry of Energy. They instructed us to address to the EPS. The analysis provided by EPS contains only information about potential benefits from the project (in general), but not the comparison against alternative models of project financing.

**4. In the process of Serbia- EU accession negotiations the emphasis should be made on international agreements which**, not only allow to avoid the procedures from domestic laws, but also limit the competition and introduce state aid, in the hidden form, through loan guarantees for state owned enterprises.

5. In relation with recommendation number 4, Transparency Serbia also recommends **proactive approach of the Commission for Control of State Aid regarding loan guarantees for state owned enterprises.**

The national program for fulfilling the EU recommendations back in 2013 had such a measure: "the Commission for Control of State Aid should pay special attention to track the allocation of state aid to public enterprises and enterprises providing services of general economic interest, in order, if state aid is not reported, to initiate proceedings and subsequent control ex officio". Transparency Serbia in the past pointed out to several examples of allocation of funds to public enterprises that had the characteristics of state aid, which the Commission did not consider (guarantees for loans to public enterprises).

## Interstate agreements and anti-corruption rules in Serbia – Constitutional aspect

The Constitution of the Republic of Serbia<sup>1</sup>, Article 194, regulates the hierarchy of national and international legal acts. Paragraph 1 stipulates that the legal system of the Republic of Serbia is unique. Paragraph 2 states that the Constitution is the supreme law of the Republic of Serbia, and paragraph 3 that all laws and other general acts enacted in Serbia must be in compliance with the Constitution. Paragraph 4 provides that **"ratified international contracts and generally accepted rules of international law" are part of the legal order of the Republic of Serbia**. Ratified international contracts **may not be contrary to the Constitution**. Finally, paragraph 5 stipulates that laws and other general acts may not be contrary to the ratified international treaties, or with the generally accepted rules of international law.

This constitutional provision provides that the agreement with a foreign state regulates the relations between the parties in a different manner than it would be the case with the application of national legislation (law) only if it is not contrary to other norms of the Constitution itself. The practice of the Constitutional Court in relation to these issues is not particularly rich. In fact, there have only been a dozen cases where the constitutionality of the provisions of an international agreement was disputed and **all these initiatives were rejected** (there were several new initiatives in 2014 and 2015, not resolved yet).

In the context of cases discussed here, particularly interesting is the decision on the rejection of the initiative that challenged the constitutionality of some provisions of the so-called "oil-gas agreement" between the Republic of Serbia and the Russian Federation. The initiative disputed the provisions of Article 9, Article 10, paragraph 2, Article 11, subparagraph 4 and Article 12 paragraph 2 of the Agreement that the National Assembly confirmed by means of the Law on Ratification of the Agreement between the Government of the Republic of Serbia and the Government of the Russian Federation on cooperation in the field of oil and gas industry ("Official Gazette of RS - International contracts", No. 83/08).

Disputed inter-state agreement regulated several instruments of cooperation between Serbia and Russia. Common interpretation of the agreement was that benefit of Serbia from that project would be stability of gas supply, through "South Stream" project, income from gas transportation tax and overall development of related industries. On the other hand, Russian company would gain dominant position in a Serbian biggest oil company under rather favourable conditions. The price paid for half of the company was approximately equal to the two years income of the company, as presented in its official financial statements<sup>2</sup>. Other benefits included low level of taxes for the extraction of Serbian oil and gas fields.

---

<sup>1</sup> [http://paragraf.rs/propisi/ustav\\_republike\\_srbije.html](http://paragraf.rs/propisi/ustav_republike_srbije.html)

<sup>2</sup> However, later reports are seriously challenging these financial statements.

Although not stated in the contract, there were interpretations in the public that this arrangement is not based only on mutual economic interest, but also political one. Namely, Serbia looked for support in its claims related to the Kosovo province, whose political leaders declared independence. In that case, Russia supported Serbian stance, while USA and most of EU did not.

Legally speaking, this set of agreements was about several different deals. If there was no interstate agreement in place, the procedure for these arrangements would significantly differ. For example, there would be open call and competitive bidding for selling of shares in Serbian NIS Company (according to the Privatization Law). As concluded by the ministry in charge representatives, "selling of shares without bidding would be illegal".

The Constitutional Court concluded that the above provisions are in accordance with the Constitution.

The Constitutional Court concluded that the provisions of the Constitution imply that ratified international contracts, according to their legal force, are located just behind the Constitution. Therefore, in the opinion of the Court, for the constitutional control of these acts the only relevant norms are the ones from the Constitution, **and there is no constitutional basis for assessing the compliance of ratified international treaties, including those that contain standards of individual character, with domestic laws.**

The Court found as compatible with the Constitution guaranteed principles of economic order and the constitutional position of the Government, the provisions of the Agreement that National Assembly confirmed by means of the Law on Ratification of the Agreement between the Government of the Republic of Serbia and the Government of the Russian Federation on cooperation in the field of oil and gas industry, which stipulate that in order to implement the project of reconstruction and modernization of the technological complex JSC "Naftna Industrija Srbije", the Serbian side is making a sale to the open joint stock company "Gazprom" or the determined affiliated party (daughter-company), a 51-percent share of participation in JSC, under the agreed conditions, on the basis that the JSC consists of the entire personally owned property from the date December 31, 2007, including (but not limited to) the facilities for the acquisition, production, refining, transportation and marketing of petroleum and petroleum products; that the selection of contractors and suppliers of material and technical resources and organizations that provide services necessary for the implementation of these projects are carried out by the Companies and JSC "Naftna Industrija Srbije" on the basis of competition (tender) and that under other equal conditions, preference is given to business entities of the States Parties; that the Serbian side for the realization of the projects listed in Article 1 of the agreement provides the retention in the period up to completion of the reconstruction and

<sup>3</sup> <http://www.transparentnost.org.rs/images/stories/inicijativeianalize/Privatizacija%20NIS%20i%20gasni%20aranzman%20sa%20Rusijom%20mart%202008.doc>

modernization of the technological complex JSC of applicable requirements in terms of quality of products produced from oil processing; that the Serbian side will consider the possibility that materials, services and works required for the realization of the projects listed in Article 1 of this Agreement are exempted from the value added tax until achieving their cost-effectiveness, as these provisions are, in the opinion of the Court, based on the provisions of the Constitution which determine that the Republic of Serbia regulates and provides its international status and relations with other countries and international organizations; single market, the legal status of business entities, the system of performing particular economic and other activities, commodity reserves, foreign economic relations, taxation system, property and obligation relations and the protection of all forms of ownership, other economic relations of public interest, sustainable development, the development of the Republic of Serbia, scientific and technological development, as well as other relations of interest for the Republic of Serbia.

The Court concluded that the Republic of Serbia is, by its Constitution, authorized to manage the property of the Republic of Serbia by means of its bodies to and perform the rights and obligations as a founder of the company, as well as to decide on sale of state assets, but the Court is not competent to assess the economic feasibility of the National Assembly decisions on the sale of that capital, nor has the responsibility to assess whether the sale of this capital is performed below its actual value. The Court also determined as consistent with the Constitution the clause in the agreement according to which the favour is given to business entities of the contracting parties under the same conditions in the tender procedure.

...

**(from the decision of the Constitutional Court, the IUM number 159/2008 of July 16, 2009, published in "Off. Gazette of RS", No. 82/2009 of October 6, 2009)**

Although the Constitutional Court is not bound by its previous decisions regarding the decision on future cases, the stated decision is diversely important from the point of testing the possible (un)constitutionality of the agreements that Serbia concluded with China, UAE and with other countries in the later period.

The first important paragraph refers to inconsistency of the international agreements with domestic legislation. In such cases there is no unconstitutionality and it is clear from the provisions of the Article 96 of the Constitution. However, it seems that the Constitutional Court does not completely close the door to assessment of the constitutionality of the norms of the international agreements that are not only contrary to domestic legislation, but also the norms of the Constitution on which these legislation is based. Problem is that the constitutional norms are not particularly detailed in elaboration of principles and they leave the questions to be regulated by laws.

Also, interesting is the decision regarding to the free market, respectively, of the Article 82 of the Constitution. In this case, assessment of constitutionality has been done in connection with the evaluation of privatization of enterprises, that is, the sale of state property, and opportunity for domestic and foreign legal entities to participate in this process, but by analogy the problem could be observed in connection with other legal matters - e.g. public procurement (which is the subject of bilateral agreements with China or public-private partnership that is the subject of agreement with UAE). Constitutional Court held opinion that such conduct is not inconsistent with the Constitution, because the state is free to dispose of its property and that the Constitution does not refer to a specific method of disposal of state property (competition). If the National Assembly has decided to dispose of state property in a certain way and if this is done by the owner of property (authorised state body), then in the Court's view, there is no violation of the Constitution, even when it is done by direct agreement and against laws which are lower legal force than the international agreement. However, it has to be emphasised that the Constitutional Court also gave some significance to the fact that the sale of public property is not the only legal business contracted by this agreement, and that it also contains other elements (cooperation between two countries in a particular area of the economy). Legal importance of this part of justification is not clear, that is, whether the provision should be unconstitutional if the agreement refers only to sale of public property.

The Agreement also includes procurement for realization of projects, from the standpoint of free and open market and equal position of foreign and domestic entities. And this is interesting from the standpoint of the agreements that Serbia has with China, because through them, it is more directly contracting that contractors will be from a particular country.

According to the assessment from the Court's justification, "market economy and open and free market, would be undermined if in tender procedure, selection of contractors is performing by favouring of certain economic entities, either through selection of those who does not meet the requirements of the competition, either in case of giving priority to contractor who offers less favourable terms". Also, "it would be unconstitutional to contract advantage of entities from the contracting countries in relation to entities from other countries, regardless of whether they meet the conditions set by the competition, i.e. under unequal conditions, and if it is envisaged only for economic entities from one country which are fulfilling the contract conditions and not for economic entities of both contracting countries".

In other words, the Court considers that it is constitutional to contract the preferential treatment of participants of competition from countries which signed the agreement (in relation to those from third countries), if they otherwise meet the conditions and if they are not unfavourable, but also the situation when the advantage to contractors were given to companies from only one country which signed the agreement. Such interpretation leaves a space for challenging the

international agreements concluded by Serbia in the meantime, because companies that will perform the works were determined in advance (e.g. the Agreement on the construction of a motorway section with Azerbaijan), or because a country of the company origin that will perform the work was determined in advance (Agreement with China).

The initiators are, among other things, pointed to possible negative consequences for the protection of the environment and the health of the population, which is a constitutional obligation of Serbia. Court considers that higher legal force of the international agreement "does not preclude the application of the general regulations on the protection of health and healthy environment, neither it abolishes the possibility to change and improve legislation in the field of environmental protection." Although this assessment the Court is correct, also the initiators had strong arguments for their claims. However, presumably a matter of respect and improvement of environmental and health standards was more factual than legal and that is why the initiative was not accepted.

Challenge of the "examination of the possibility... of exemption from value added tax." Constitutional Court has held opinion that the Constitution does not regulate directly tax incentives and exemptions, and that therefore neither the norm can be unconstitutional. To remind, the Agreement with China (as well as agreements with some other countries and international organizations) includes not just optional, but mandatory exemption from tax.

In overall the problem of the system, as it could be concluded on the basis of this decision is absence of constitutional provisions that would limit the will of the Parliament. If the implementation of direct negotiation in dealing with public assets cannot be challenged and if it is not possible to oppose legally decisions of the parliament and government for their damageable economic effects, it means that Constitution does not protect from such damages however big they are. Theoretically, the Parliament may agree to sell for 1 USD only all public property or to take 1000 Billion USD loan under whatever conditions. If being part of inter-state agreement, such a decision would be considered in accordance with the Constitution.

## Stabilisation and Association Agreement

Stabilisation and Association Agreement (SAA) is an international contract, signed on April 29th in 2008, between the Republic of Serbia and European Union. Two most important obligations that Republic of Serbia overtakes with this agreement will be establishing of the free trade zone and harmonization of the legislation of the Republic of Serbia with EU law.

Agreement creates free trade zone between Serbia and EU in the transitional period of six years. Deadline for trade liberalization is defined taking into consideration the capability of Serbian industry and agriculture to adjust to free trade but also with the desire of Serbia for faster ending of the reforms and accessing European Union. Obligation of Serbia is to gradually abolish customs tariffs to import of merchandise originating from European Union in transitional period.

On the other hand, with this contract, European Union confirms free access to merchandise from Serbia to European Union market.

The rate of liberalization and level of protection depend on degree of sensitivity of products for Serbian industry. Three groups of industry products are defined, by grading the sensitivity, for which the liberalization will occur after the period of two, five or six years. For the products that are not listed, custom tariffs will be abolished at the moment when this agreement becomes effective. It is provided for the key sectors of the domestic industry (like car industry, toys, footwear, ceramics, etc.) to remain highly protected during the transitional period of five or six years.

Stabilization and Association Agreement envisages harmonization of the domestic legislation with the acquis of the European communities as an obligation of the Republic of Serbia. Having in mind the scope of acquis, priority areas that create direct impact to creating the zone of free trade between the EU and Serbia are defined: protection of competition and control of state aid (subsidies), intellectual property rights, public procurements, standardization and consumer protection<sup>4</sup>.

Stabilisation and Association Agreement between the European Communities and their Member States of the one part, and the Republic of Serbia, of the other part ("Official Gazette of the RS - International Contracts", no. 83/2008), signed on April 29<sup>th</sup> 2008 in Luxembourg. Serbia ratified it on 10 September 2008. However, although Serbia started implementation ("unilaterally") of the transitional trade agreement immediately, the complete SAA became effective only on 1 September 2013, on the basis of Announcement of the Date of Stabilization and Association

---

<sup>4</sup> Up to this line taken from the web-site of the European Integration Office of the Government of Serbia. <http://www.seio.gov.rs/%D0%B4%D0%BE%D0%BA%D1%83%D0%BC%D0%B5%D0%BD%D1%82%D0%B0%D1%81%D0%BF%D0%BE%D1%80%D0%B0%D0%B7%D1%83%D0%BC%D0%B8.151.html>

Agreement Between the European Communities and their Member States of the one part and the Republic of Serbia of the other part, becoming effective, that was published in the "Official Gazette of the RS - International Contracts", no. 11/2013 on 24 September 2013.

Text below will list or describe some of the provisions of this agreement that can be related to implementation of interstate contracts discussed in more details in case studies.

Preamble, among other, mentions that Agreement is signed CONSIDERING the commitment of the Parties to free trade, in compliance with the rights and obligations arising out of membership of the WTO;

Goals of association are following:

### **ARTICLE 1**

*1. The aims of this Association are:*

- (a) *to support the efforts of Serbia to strengthen democracy and the rule of law;*
- (b) *to contribute to political, economic and institutional stability in Serbia, as well as to the stabilisation of the region;*
- (c) *to provide an appropriate framework for political dialogue, allowing the development of close political relations between the Parties;*
- (d) *to support the efforts of Serbia to develop its economic and international cooperation, including through the approximation of its legislation to that of the Community;*
- (e) *to support the efforts of Serbia to complete the transition into a functioning market economy;*
- (f) *to promote harmonious economic relations and gradually develop a free trade area between the Community and Serbia;*
- (g) *to foster regional cooperation in all the fields covered by this Agreement.*

Article 8. stipulates on gradual association and supervision, and article 9 refers to international agreements:

### **ARTICLE 8**

*The association shall be progressively and fully realised over a transitional period of a maximum of six years.*

*The Stabilisation and Association Council (hereinafter also referred to as "SAC") established under Article 119 shall regularly review, as a rule on an annual basis, the implementation of this Agreement and the adoption and implementation by Serbia of legal, administrative, institutional and economic reforms. This review shall be carried out in the light of the preamble and in accordance with the general principles of this Agreement. It shall take duly into account priorities*

*set in the European Partnership relevant to this Agreement and be in coherence with the mechanisms established under the Stabilisation and Association process, notably the progress report on the Stabilisation and Association process.*

*On the basis of this review, the SAC will issue recommendations and may take decisions. Where the review identifies particular difficulties, they may be referred to the mechanisms of dispute settlement established under this Agreement.*

*The full association shall be progressively realised. No later than the third year after the entry into force of this Agreement, the SAC shall make a thorough review of the application of this Agreement. On the basis of this review the SAC shall evaluate progress made by Serbia and may take decisions governing the following stages of association.*

*The aforementioned review will not apply to the free movement of goods, for which a specific schedule is foreseen in Title IV.*

## **ARTICLE 9**

*This Agreement shall be fully compatible with and implemented in a manner consistent with the relevant WTO provisions, in particular Article XXIV of the General Agreement on Tariffs and Trade 1994 (GATT 1994) and Article V of the General Agreement on Trade in Services (GATS).*

The chapter on free movement of goods stipulates the custom tariffs that will be gradually abolished in the period of six years. However, it is not about custom politics towards third countries.

Similarly, chapter on industrial products stipulates the exchange of products that originate from EC or Serbia, but not the goods coming from the third countries.

Chapter III – General provisions, envisage prohibition of fiscal discrimination.

## **ARTICLE 37 - Prohibition of fiscal discrimination**

*1. The Community and Serbia shall refrain from, and abolish where existing, any measure or practice of an internal fiscal nature establishing, whether directly or indirectly, discrimination between the products of one Party and like products originating in the territory of the other Party.*

*2. Products exported to the territory of one of the Parties may not benefit from repayment of internal indirect taxation in excess of the amount of indirect taxation imposed on them.*

Provisions of the article 37 para 2 of the Agreement envisage prohibition of discrimination that refers to products that originate from Serbia or EC, but not related to products originating from third countries that are imported to Serbia or EC. Article 39 defines customs unions, free trade areas, and cross-border arrangements:

***ARTICLE 39 - Customs unions, free trade areas, cross-border arrangements***

*1. This Agreement shall not preclude the maintenance or establishment of customs unions, free trade areas or arrangements for frontier trade except in so far as they alter the trade arrangements provided for in this Agreement.*

*2. During the transitional period specified in Article 18, this Agreement shall not affect the implementation of the specific preferential arrangements governing the movement of goods either laid down in frontier Agreements previously concluded between one or more Member States and Serbia or resulting from the bilateral Agreements specified in Title III concluded by Serbia in order to promote regional trade.*

*3. Consultations between the Parties shall take place within the Stabilisation and Association Council concerning the Agreements described in paragraphs 1 and 2 of this Article and, where requested, on other major issues related to their respective trade policies towards third countries. In particular in the event of a third country acceding to the Union, such consultations shall take place so as to ensure that account is taken of the mutual interests of the Community and Serbia stated in this Agreement.*

One gets the impression that this is primarily about protection of existing privileged arrangements in regional level (e.g. CEFTA agreement), and not about relations that Serbia establishes with more distant countries. Anyways, freedom of providing privileges to third countries is not limited unless it disturbs trade arrangements from the SAA.

Measures of protection through trade measures in case of dumping and subsidies that influence the implementation of the SAA are stipulated in the article 40:

***ARTICLE 40 - Dumping and subsidy***

*1. None of the provisions in this Agreement shall prevent any of the Parties from taking trade defence action in accordance with paragraph 2 of this Article and Article 41.*

*2. If one of the Parties finds that dumping and/or countervailable subsidisation is taking place in trade with the other Party, that Party may take appropriate measures against this practice in*

*accordance with the WTO Agreement on Implementation of Article VI of the GATT 1994 or the WTO Agreement on Subsidies and Countervailing Measures and the respective related internal legislation.*

Although article 40 leads to possible wider implementation, article 41 para 2 states only certain manifestations of harmful actions – excessive import of certain product that causes difficulties to the economy of the one signatory party.

Articles 59 and 60 deal with providing of services. They guarantee protection of “the existing situation“, the rights of legal entities from the Community to provide certain services in Serbia (and vice versa). In theory, interstate agreements with third countries could lead to situation like this, for example, if the services of certain kind, that were previously available to companies from EC, were awarded by interstate agreement of the Republic of Serbia exclusively to companies from third countries. Provision stipulates:

#### **ARTICLE 60**

*1. The Parties shall not take any measures or actions which render the conditions for the supply of services by Community and Serbia nationals or companies which are established in a Party other than that of the person for whom the services are intended significantly more restrictive as compared to the situation existing on the day preceding the day of entry into force of this Agreement.*

*2. If one Party is of the view that measures introduced by the other Party since the entry into force of this Agreement result in a situation which is significantly more restrictive in respect of supply of services as compared with the situation existing at the date of entry into force of this Agreement, such first Party may request the other Party to enter into consultations.*

Chapter V, title VI **Approximation of laws, law enforcement and competition rules**, defines several important matters. Article 72 stipulates generally on harmonization of laws of Serbia with the EC Laws (that will be performed gradually):

#### **ARTICLE 72**

*1. The Parties recognise the importance of the approximation of the existing legislation in Serbia to that of the Community and of its effective implementation. Serbia shall endeavour to ensure that its existing laws and future legislation will be gradually made compatible with the Community acquis. Serbia shall ensure that existing and future legislation will be properly implemented and enforced.*

*2. This approximation shall start on the date of signing of this Agreement, and shall gradually extend*

*to all the elements of the Community acquis referred to in this Agreement by the end of the transitional period defined in Article 8 of this Agreement.*

*3. Approximation will, at an early stage, focus on fundamental elements of the Internal Market acquis, Justice, Freedom and Security as well as on other trade-related areas. At a further stage, Serbia shall focus on the remaining parts of the acquis.*

*Approximation shall be carried out on the basis of a programme to be agreed between the European Commission and Serbia.*

*Serbia shall also define, in agreement with the European Commission, the detailed arrangements for the monitoring of the implementation of approximation of legislation and law enforcement actions to be taken.*

Article 73 speaks of competition:

#### ***ARTICLE 73- Competition and other economic provisions***

*1. The following are incompatible with the proper functioning of this Agreement, insofar as they may affect trade between the Community and Serbia:*

- (I) all Agreements between undertakings, decisions by associations of undertakings and concerted practices between undertakings which have as their object or effect the prevention, restriction or distortion of competition;*
- (ii) abuse by one or more undertakings of a dominant position in the territories of the Community or Serbia as a whole or in a substantial part thereof;*
- (iii) any State aid which distorts or threatens to distort competition by favouring certain undertakings or certain products.*

*2. Any practices contrary to this Article shall be assessed on the basis of criteria arising from the application of the competition rules applicable in the Community, in particular from Articles 81, 82, 86 and 87 of the EC Treaty and interpretative instruments adopted by the Community institutions.*

*3. The Parties shall ensure that an operationally independent authority is entrusted with the powers necessary for the full application of paragraph 1(i) and (ii) of this Article, regarding private and public undertakings and undertakings to which special rights have been granted.*

*4. Serbia shall establish an operationally independent authority which is entrusted with the powers necessary for the full application of paragraph 1 (iii) within one year from the date of entry into force of this Agreement. This authority shall have, inter alia, the powers to authorise State aid schemes*

*and individual aid grants in conformity with paragraph 2, as well as the powers to order the recovery of State aid that has been unlawfully granted.*

*5. The Community on one side and Serbia on the other side shall ensure transparency in the area of State aid, inter alia by providing to the other Parties a regular annual report, or equivalent, following the methodology and the presentation of the Community survey on State aid. Upon request by one Party, the other Party shall provide information on particular individual cases of public aid.*

*6. Serbia shall establish a comprehensive inventory of aid schemes instituted before the establishment of the authority referred to in paragraph 4 and shall align such aid schemes with the criteria referred to in paragraph 2 within a period of no more than 4 years from the entry into force of this Agreement.*

*7. (a) For the purposes of applying the provisions of paragraph 1 (iii), the Parties recognise that during the first five years after the entry into force of this Agreement, any public aid granted by Serbia shall be assessed taking into account the fact that Serbia shall be regarded as an area identical to those areas of the Community described in Article 87(3) (a) of the EC Treaty.*

*(b) Within four years from the entry into force of this Agreement, Serbia shall submit to the European Commission its GDP per capita figures harmonised at NUTS II level. The authority referred to in paragraph 4 and the European Commission shall then jointly evaluate the eligibility of the regions of Serbia as well as the maximum aid intensities in relation thereto in order to draw up the regional aid map on the basis of the relevant Community guidelines.*

*8. As appropriate, Protocol 5 establishes the rules on state aid in the steel industry. This Protocol establishes the rules applicable in the event restructuring aid is granted to the steel industry. It would stress the exceptional character of such aid and the fact that the aid would be limited in time and would be linked to capacity reductions within the framework of feasibility programmes.*

*9. With regard to products referred to in Chapter II of Title IV:*

*(a) paragraph 1(iii) shall not apply;*

*(b) any practices contrary to paragraph 1(i) shall be assessed according to the criteria established by the Community on the basis of Articles 36 and 37 of the EC Treaty and specific Community instruments adopted on this basis.*

*If one of the Parties considers that a particular practice is incompatible with the terms of paragraph 1, it may take appropriate measures after consultation within the Stabilisation and Association Council or after 30 working days following referral for such consultation. Nothing in this Article shall prejudice or affect in any way the taking, by the Community or Serbia, of countervailing measures in accordance with the GATT 1994 and the WTO Agreement on Subsidies and*

*Countervailing Measures and the respective related internal legislation.*

Which of these can be relevant for implementation of interstate agreements? Primarily, it is important to mention that all of the stated forms of harmful behaviour are prohibited only in a level that can affect the trade between EC and Serbia, as well as that such proceedings are evaluated only in relation to criteria implemented in the EU.

Those are cartel agreements between companies, abuse of dominant position and state aid that undermines or threatens to undermine competition. Interstate agreements can have provisions on state aid and often they make such arrangements.

With paragraph 4 Serbia obliges to establish „operational independent body“ with corresponding duties. That is Commission for State Aid Control, established on the principle of interdepartmental body with insufficiently clear legal status in the state administration system. Para 5 stipulated obligation of „transparency“, i. e. delivering of annual report on awarded state aid to counterparty, and to the request of counterparty also about „certain individual cases of public aid“.

Article 76 organizes public procurements in following manner:

### ***ARTICLE 76 - Public procurement***

*1. The Community and Serbia consider the opening-up of the award of public contracts on the basis of non-discrimination and reciprocity, following in particular the WTO rules, to be a desirable objective.*

*2. Serbian companies, whether established in the Community or not, shall be granted access to contract award procedures in the Community pursuant to Community procurement rules under treatment no less favourable than that accorded to Community companies as from the entry into force of this Agreement.*

*The above provisions shall also apply to contracts in the utilities sector once the government of Serbia has adopted the legislation introducing the Community rules in this area. The Community shall examine periodically whether Serbia has indeed introduced such legislation.*

*3. Community companies established in Serbia under the provisions of Chapter II of Title V shall, from the entry into force of this Agreement, be granted access to contract award procedures in Serbia under treatment no less favourable than that accorded to Serbian companies.*

*4. Community companies not established in Serbia shall be granted access to contract award procedures in Serbia pursuant to the Serbian Law on Public Procurement under treatment no less favourable than that accorded to Serbian companies at the latest five years after the entry into force of this Agreement.*

*Upon the entry into force of this Agreement, Serbia shall convert any existing preference for domestic economic entities to a price preference and, within a period of five years, shall gradually reduce the latter in accordance with the following timetable:*

*- the preferences shall not exceed 15 % by the end of the second year following the entry into force of this Agreement;*

*- the preferences shall not exceed 10 % by the end of the third year following the entry into force of this Agreement;*

*- the preferences shall not exceed 5 % by the end of the fourth year following the entry into force of this Agreement; and*

*- the preferences will be completely abolished no later than the end of the fifth year following the entry into force of this Agreement.*

*5. The Stabilisation and Association Council shall periodically examine the possibility for Serbia to introduce access to contract award procedures in Serbia for all Community companies. Serbia shall report annually to the Stabilisation and Association Council on the measures they have taken to enhance transparency and to provide for effective judicial review of decisions taken in the area of public procurement.*

*6. As regards establishment, operations, supply of services between the Community and Serbia, and also employment and movement of labour linked to the fulfilment of public contracts, the provisions of Articles 49 to 64 are applicable.*

Greatest attention in this Article is given to matters of advantages of Serbian companies and products with Serbian origin in domestic market compared to companies from the EU. This does not refer to potential advantage given to companies and goods from third countries. From the standpoint of interstate agreements, more important is the provision that has more general character that is implemented to all public procurements in Serbia. Para 4 stipulates that companies from EU have access to information (i. e. possibility to participate in the public procurement procedures) „in compliance with the Public Procurement Law“ and „under conditions not less favourable than the conditions implemented to Serbian business companies“, after expiration of certain period of time (five years).

Even when this obligation of SAA would be completely effective, it could not be considered that Serbia has violated the rule with recent interstate agreements.

Namely, there are such agreements where it is agreed in advance that contractor will be from the country that provides the credit (e. g. China, Azerbaijan). In such clauses, companies from the EU are in equal position as the companies from the Republic of Serbia, therefore SAA is not violated. Other option is that interstate agreement provides advantage to companies from Serbia and third country (e. g. China, Russia) in regards to companies from the rest of the world (including EU). Then, companies from the EU would undoubtedly be damaged. However, since the “access to public procurement procedures” is “in compliance with the Public Procurement Law”, and Public Procurement Law, in article 7 stipulates that it will not be effective when the procurement is being organized on the basis of interstate agreement, therefore, this could not be a reason for contestation of interstate agreement on the basis of SAA.

Provisions of the article 93 of the SAA on foreign investments are important for certain interstate agreements. Provision is of general character and does not provide efficient protection to investors from the EU compared to those coming from third countries in situations where significant advantage is given to investors from third countries in doing business in Serbia (e. g. agreements with UAE):

#### ***ARTICLE 93 - Investment Promotion and Protection***

*Cooperation between the Parties, within the scope of their respective competencies, in the field of investment promotion and protection shall aim to bring about a favourable climate for private investment, both domestic and foreign, which is essential to economic and industrial revitalisation in Serbia. The particular aims of cooperation shall be for Serbia to improve the legal frameworks which favours and protects investment.*

Article 94 defines industrial cooperation, without providing special rights to companies from EU in case of certain interstate agreements between Serbia and third countries that would be privileged in such situation:

#### ***ARTICLE 94 - Industrial Cooperation***

*Cooperation shall aim to promote the modernisation and restructuring of industry and individual sectors in Serbia. It shall also cover industrial cooperation between economic operators, with the objective of strengthening the private sector under conditions which ensure that the environment is protected. Industrial cooperation initiatives shall reflect the priorities determined by both Parties. They shall take into account the regional aspects of industrial development, promoting transnational partnerships when relevant. The initiatives should seek in particular to establish a suitable framework for undertakings, to improve management, know-how and to promote markets, market transparency and the business environment. Special attention shall be devoted to the establishment*

*of efficient export promotion activities in Serbia. Cooperation shall take due account of the Community acquis in the field of industrial policy.*

Only article 109 refers to energy area. This article that remains only at the level of principle, states the issues of cooperation between Serbia and the EU in energy field, but doesn't present stronger obstacles (besides potential political consequences in the form of negative evaluation on preparedness for association) for Serbia to choose some different method (if it doesn't promote energy efficiency, doesn't perform diversification of supplies):

### ***ARTICLE 109 - Energy***

*Cooperation shall focus on priority areas related to the Community acquis in the field of energy. It shall be based on the Treaty establishing the Energy Community, and it shall be developed with a view to the gradual integration of Serbia into Europe's energy markets. Cooperation may include in particular:*

*(a) the formulation and planning of energy policy, including modernisation of infrastructure, improvement and diversification of supply and improvement of access to the energy market, including facilitation of transit, transmission and distribution and restoration of energy interconnections of regional importance with neighbouring countries;*

*(b) the promotion of energy saving, energy efficiency, renewable energy and studying the environmental impact of energy production and consumption;*

*(c) the formulation of framework conditions for restructuring of energy companies and cooperation between undertakings in this sector.*

Similarly, article on the protection of environment (article 111), defines cooperation of Serbia and the EU in this field, but doesn't stipulate strict obligations of the Serbia to make some specific steps, whose violation would represent violation of the SAA. It seems that the only consequence of “dissonant” policy in regards to protection of the environment can be “political”– negative evaluation of the progress in this area:

### ***ARTICLE 111 - Environment***

*The Parties shall develop and strengthen their cooperation in the environmental field with the vital task of halting further degradation and start improving the environmental situation with the aim of sustainable development.*

*The parties shall, in particular, establish cooperation with the aim of strengthening administrative structures and procedures to ensure strategic planning of environment issues and coordination*

*between relevant actors and shall focus on the alignment of Serbia's legislation to the Community acquis. Cooperation could also centre on the development of strategies to significantly reduce local, regional and trans-boundary air and water pollution, to establish a framework for efficient, clean, sustainable and renewable production and consumption of energy, and to execute environmental impact assessment and strategic environmental assessment. Special attention shall be paid to the implementation of the Kyoto Protocol.*

Within the Title X - institutional, general and final provisions, the Stabilisation and Association Council has been established which shall supervise the application and implementation of this Agreement. The task of the Council is to examine any major issues arising within the framework of this Agreement and any other bilateral or international issues of mutual interest. The Council consists of members of the Council of the EU, the EC and the Government of Serbia. In matters that concern it, the European Investment Bank shall take part, as an observer, in the work of the Stabilisation and Association Council.

In order to achieve the objectives of this Agreement, the Stabilisation and Association Council has the power to take decisions within the scope of this Agreement, in the cases provided for therein. The decisions taken shall be binding on the Parties, which will have to take measures necessary for their implementation. The Stabilisation and Association Council may also make appropriate recommendations. The Council shall draw up its decisions and recommendations by agreement between the parties.

The Stabilisation and Association Council shall be assisted in the performance of its duties by a Stabilisation and Association Committee, composed of representatives of the Council of the European Union and of representatives of the European Commission, on the one hand, and of representatives of the Government of Serbia on the other. The Stabilisation and Association Council may delegate to the Stabilisation and Association Committee any of its powers. The Stabilisation and Association Committee may create subcommittees. The Stabilisation and Association Council may decide to set up other special committees or bodies that can assist it in carrying out its duties.

Also, the Stabilisation and Association Parliamentary Committee has been established. It is a forum for Members of the Parliament of Serbia and of the European Parliament to meet and exchange views. It shall meet at intervals that it shall itself determine.

Serbia and the EU had agreed to take all measures needed to fulfill obligations and objectives of the SAA, to consult with purpose to discuss issues that require interpretation, to refer to the Stabilisation and Association Council any dispute related to the interpretation (that the Council may adopt a decision which has the binding effect).

If either Party considers that the other Party has failed to fulfil an obligation under this Agreement, it may take appropriate measures. Before so doing, except in cases of special urgency, it shall supply the Stabilisation and Association Council with all relevant information required for a thorough examination of the situation with a view to seeking a solution acceptable to the Parties. In the selection of measures, priority must be given to those which least disturb the functioning of this Agreement.

When a dispute arises between the Parties concerning the interpretation or the implementation of this Agreement, any Party shall notify to the other Party and the Stabilisation and Association Council a formal request that the matter in dispute be resolved.

Where a Party considers that a measure adopted by the other Party, or a failure of the other Party to act, constitutes a breach of its obligations under this Agreement, the formal request that the dispute be resolved shall give the reasons for this opinion and indicate, as the case may be, that the Party may adopt measures as provided for in the SAA.

As long as the dispute is not resolved, it shall be discussed at every meeting of the Stabilisation and Association Council, unless the arbitration procedure as provided for in Protocol 7 has been initiated (dispute settlement). A dispute shall be deemed to be resolved when the Stabilisation and Association Council has taken a binding decision to settle the matter or when it has declared that there is no dispute anymore.

Consultations on a dispute can also be held at any meeting of the Stabilisation and Association Committee or any other relevant committee or body set up on the basis of Articles 123 or 124, as agreed between the Parties or at the request of any of the Parties. Consultations may also be held in writing. All information disclosed during the consultations shall remain confidential.

The SAA is concluded for an unlimited period. Either Party may denounce this Agreement by notifying the other Party. This Agreement shall terminate six months after the date of such notification. Either Party may suspend this Agreement, with immediate effect, in the event of the non-compliance by the other Party of one of the essential elements of this Agreement.

### **Consideration of the SAA application**

In present practice of the SAA application, at least according to the available reports from meetings, the existence of some disputed issues was not mentioned, neither the endanger of the SSP through the provisions of international agreements<sup>5</sup>.

---

<sup>5</sup> <http://europa.rs/drugi-sastanak-saveta-za-stabilizaciju-i-privredizivanje-izmedu-srbije-i-eu/>  
<http://europa.rs/drugi-sastanak-odbora-za-stabilizaciju-i-privredizivanje-eu-i-srbije/>

From the above analysis it can be concluded that the norms of international agreements that Serbia has so far concluded with third countries are not contrary to those parts of the SAA which stipulate explicit obligations or restrictions for Serbia. The only exception may represent some actions which are, on the basis of bilateral agreements, providing state aid to enterprises. In this respect, one of violations of the SAA was also ascertain in the Progress Report for Serbia for 2014 – that the report on granted state aid has not be delivered. However, with regards to certain areas, such as energy or foreign investments, where in the SAA, instead of prohibitions and obligations, principles of cooperation were determined, the situation may arise in which treatment of Serbia could be assessed as incompatible with objectives which are underlying the SAA conclusion.

Although the possible violations of the SAA through other international agreements can be reviewed by the competent Council, Committee and other bodies, the big question is whether they can be subject of dispute before the national institutions. Namely, the SAA and other international agreements have, in principle, the same legal force in the hierarchy of legal acts of the Republic of Serbia. In the absence of other rules, it could be claimed that the will of the legislature, expressed through the ratification of the latter agreement, represent the intention to make ineffective the norm from the former agreement which is contrary to it. Such initiatives, as far as it is we know, has not yet been before the Constitutional Court.

## **The review of the agreements between the Republic of Serbia and the People's Republic of China and the reasons for their adoption**

The law that confirmed the loan agreement for the construction of block B thermal power plant in Kostolac, was adopted in 2015<sup>6</sup>. This loan was confirmed by the Supervisory Board of EPS (Serbian state owned electricity company whose legal form is "public enterprise" - PE) on March 15, 2015<sup>7</sup>.

This law confirmed the loan agreement for the privileged buyer's credit for the second phase of the project package "Kostolac B Power Plant Project". The contract was concluded between the Government of the Republic of Serbia, represented by the Ministry of Finance as the borrower and Chinese Export-Import Bank as the lender. The contract was concluded on December 17, 2014. The original contract in English language and the Law on ratification includes a translation of the contract to Serbian language.

As a constitutional basis for the confirmation of the loan agreement, the explanatory note specifies the provision of Article 99, paragraph 1, item 4 of the Constitution of the Republic of Serbia, which stipulates that the National Assembly ratifies international agreements when the Law predicts the obligation of their ratification. Such an obligation is provided in the provision of Article 5, paragraph 2 of the Law on Public Debt ("Official Gazette of RS", No. 61/05, 107/09 and 78/11), according to which the National Assembly of the Republic of Serbia decides on the indebtedness of the Republic of Serbia.

Furthermore, this contract is based on the **Agreement on economic and technical cooperation in the field of infrastructure between the Government of the Republic of Serbia and the Government of the People's Republic of China**, signed on August 20, 2009 and published in the "Official Gazette of RS - International agreements, No. 90/09, 9/13, 11/13 and 13/13. As stated in the explanation of the draft law, *"several significant projects in the Republic of Serbia is successfully implemented on the basis of this international agreement, which are financed through favourable credit lines of Chinese Export-Import Bank as the authorized institution of the People's Republic of China Government."*

Article 11 of the above-mentioned agreement stipulates that, among other things, the cooperation will take place through the delivery of the works, materials and services for the construction of power plants, which on July 22, 2010 resulted in the conclusion of the General contractual agreement on the realization of the Project Package KOSTOLAC-B Power Plant

---

<sup>6</sup> <http://www.parlament.gov.rs/upload/archive/files/lat/pdf/zakoni/2015/37-15%20lat.pdf>

<sup>7</sup> <http://www.ekapija.com/website/sr/page/1094105>

Projects between PE "Elektroprivreda Srbija", PE "Termoelektrane i kopovi Kostolac" and the Chinese company China National Machinery & Equipment Import & Export Corporation (CMEC) from Beijing (contracting parties). The agreed phase implementation of the project package KOSTOLAC-B Power Plant Projects (hereinafter: Package project) related to:

1. Revitalization of two existing blocks B1 and B2, of 350 MW each;
2. Desulphurization project for two existing blocks B1 and B2, of 350 MW each;
3. The project to increase the capacity of open mine Drmno to 12 million tons per year with the construction of new block B3.

It was agreed that the Package Project is implemented in two phases, so that the first phase includes works on revitalization of two existing blocks B1 and B2 and their desulphurization, with the corresponding infrastructure for the construction of railway and modernization of port and road, located in the vicinity of the town of Kostolac, while increasing the capacity of open mine Drmno with the construction of new block B3 is covered by the second phase of works. The approximate price for the implementation of Project Package was agreed in the amount of \$ 1,060,230,000, of which \$ 344,630,000 related to the value of the first phase, and \$ 715,600,000 to the value of the second phase, so that, in the meantime, the contracting parties concluded two single contracting agreements, for each phase separately, on the basis of which the Chinese Export-Import Bank submitted requests for the use of favourable credit lines for privileged buyer.

Acting on the Resolution of the Government 05 No. 312-8779/2010-1 of December 2, 2010, the contracting parties first concluded a contractual agreement for the first phase of the Project Package on December 8, 2010 in the amount of \$ 344,630,000, for the financing of which the Republic of Serbia has already been approved a loan of \$ 293 million, covering 85% of the project whose realization is assessed as successful, as until today more than 50% of the approved funds has been withdrawn. The remaining 15% is funded from personal resources of "Elektroprivreda Srbija", as the commissioner and PE "TE-KO Kostolac, as the end user.

In 2012, the Government of the People's Republic of China, with the Chinese Foreign Ministry, formed the Secretariat for the cooperation between China and the countries of Central and Eastern Europe and granted a special credit line of \$ 10 billion for the improvement of cooperation with these countries, inviting all countries to nominate the projects for obtaining favourable loans through the Export-Import Bank. In response to the invitation of the Chinese party, the Serbian government proposed the continuation of cooperation with the Chinese company CMEC on the second phase of the Project Package, which on November 20, 2013 resulted in the conclusion of the contractual agreement for the second phase of the Project Package (contractual agreement), at a price of \$ 715,600,000. It is further stated that **the financial analysis performed on the basis of cost-effectiveness Study showed that the**

**implementation of the second phase is economically viable and cost-effective**, after which, on the basis of the Government Resolution 05 No. 48-10165/2013 of November 28, 2013, a loan application was submitted to China Export-Import Bank, with supporting documents, which requested the approval of the loan under preferential conditions in the amount of \$ 608,260,000 to finance 85% of the value of the second phase of the Project Package. The remaining \$ 107.34 million (15% of the contract value), will be financed by PE "Elektroprivreda Srbije", as the commissioner and PE "TE-KO Kostolac, as the end user, from their own resources.

By the Conclusion 05 No. 48-16044/2011 of December 15, 2014 the Government adopted a draft loan agreement and at the same time authorized PhD Dusan Vujovic, the Minister of Finance, to sign the contract on behalf of the Government and as a representative of the Republic of Serbia. The loan agreement was signed on December 17, 2014 in Belgrade, during the 3rd Summit of Heads of State of China Ciez.

The explanation states that the Law on Budget of the Republic of Serbia for 2014 ("Official Gazette of RS", No. 110/13, 116/14 and 142/14) **has already planned the borrowing of the Republic of Serbia at the Chinese Export-Import Bank** for the implementation of the second phase of the Package Project TE-KO Kostolac (the construction of the new energy block at the location Drmno and the expansion of the capacity of mines) in the amount of \$ 608,260,000, which corresponds to 85% of the contractual value of this phase. It is noted that the Law on Budget of the Republic of Serbia for 2015 ("Official Gazette of RS", No. 142/14) provides the same indebtedness.

The explanation states that the funds for the implementation of the contract would be provided by the budget of the Republic of Serbia.

The preamble to the contract contains a reference to the Agreement on economic and technical cooperation in the field of infrastructure (the Agreement on economic and technical cooperation), which entered into force on June 25, 2010. This agreement was signed by the Governments of China and Serbia on August 20, 2009.

### **Previous agreements**

General Agreement on economic and technical cooperation in the field of infrastructure between the Government of the Republic of Serbia and the Government of the People's Republic of China, from 2009, with amendments from 2013, in the preamble states, among other things, that the goal is "improving cooperation ... **in accordance with their national legislation and the provisions of this Agreement.**" In other words, the Agreement should be interpreted in such a way that a deviation from the national legislation is seen as an exception instead of a goal, and which is possible on the basis of the agreement.

The agreement has a number of areas, some of which are broadly defined, so that they can significantly affect the application of national legislation:

The first activity is defined as the Development and implementation of infrastructure projects. All other activities are related to this one (preparing studies for infrastructure, experts' technical assistance, purchase of machinery, equipment and materials, and services necessary to build and maintain infrastructure projects, exchange of experiences in terms of signaling and integrated systems and other forms of cooperation in the field of infrastructure projects suggested by any of the parties).

All of these activities may affect the application of the regulations of the Republic of Serbia, and especially of the Public Procurement Law, the Law on Public-Private Partnerships and the Law on State Aid Control.

Article 5 of the basic Agreement more specifically governs the exemptions from the application of Public Procurement Law and the Law on PPE. This is achieved by anticipating that the relevant Chinese trade associations **can suggest qualified contractors for participation in projects**, and that a list of recommended contractors for each project is submitted to the country which implements the project.

Article 5 does not exclude the automatic application of the entire Law on Public Procurement, but exempts its key provisions, stipulating that "agreements, contracts, programs and projects prepared in accordance with this Agreement on the territory of the Republic of Serbia **are not subject to the announcement of a public tender for performing investment projects and delivery of goods and services, unless otherwise specified by a commercial contract**. Therefore, competition may be applied, but only if it is planned by a specific agreement. Besides the non-application of Public Procurement Law of the Republic of Serbia, these provisions exclude the obligation of tenders on some other basis and in some other ways (e.g. by the application of Chinese regulation or some other procedure). As noted above, Article 7 of the Law on Public Procurement indicates that this Law is not applied when procurement is implemented on the basis of an interstate agreement.

The agreement also includes standards on subcontractors. Unlike the Public Procurement Law which obliges the bidder to indicate subcontractors, this issue is resolved by means of solutions from each commercial contract. It can also be achieved by a procedure of competition between companies in Serbia that are interested in doing business with the project leader - a company from the People's Republic of China.

Article 6 excluded the payment of customs duty and value added tax in connection with the

exercise of agreements, contracts, programs and projects.

The explanation specifically states that the project financing is carried out in cases when there is no international auction for these projects.

It is interesting that one of the listed arguments for the conclusion of this agreement is the "big deficit of Serbia in trade with China." It remains unclear in what way could these deficits be reduced by bringing Chinese investments to Serbia according to the adopted model, since this model involves the procurement of goods from China, paying the Chinese companies to carry out the works and the like. It was also stated that the construction of motorway infrastructure facilities is of strategic importance for the Republic of Serbia, and that the loan conditions would be favorable (without additional information).

All the laws were adopted by urgent procedure, which leaves less time for the deputies to consider the text of the contract. According to the Government Rules of Procedure, international agreements carry no obligation to conduct a public debate in the preparation of regulations, under which the citizens could give their opinion on the proposed regulations. The reason for this is the inability to change the agreement after signing it. However, the public debate could serve to examine the compliance of the agreement with the rest of the legal system and its good or bad sides.

It is interesting to note that the Annex No. 1 was applied without ratification for more than a year.

Both the basic agreement and the two Annexes were proposed for ratification stating that they do not create obligations for the budget of the Republic of Serbia. This assertion is fundamentally incorrect, especially for Annex 2, which stipulates the exemption from VAT and customs duties and which necessarily reflects in the future budget revenues.

The explanations of these draft laws still lack a mandatory part - the statement of compliance with European Union regulations.

Specifically, Article 39a, par. 1 and 2 of the Government Rules of Procedure stipulate that "along with the draft law and the draft regulation, a proponent needs to submit Annexes in the form of EU Regulatory Compliance Statement and EU Regulatory Compliance Table, on the forms that are regulated by a special act of the Government". Also, it is further stipulated that "EU Regulatory Compliance Statement and EU Regulatory Compliance Table need to be submitted with the proposal of the decision that regulates the legislation of the Republic of Serbia in accordance with the legislation of the European Union".

There are no planned sanctions in case of violation of this obligation by the ministry that prepares the draft law on ratification of international agreements - such a document could be adopted by the Government as a draft law and submitted to the Parliament. As a result, the members of the Government, then the deputies, and finally all citizens remain left without an important insight on whether the treaties whose ratification is proposed is in any way contrary to EU rules, or the undertaken commitments under the SAA.

## **Agreements with China, the application of the laws of the Republic of Serbia, the economic and other effects**

### **Are the agreements with China economically feasible?**

The explanation of the loan agreement for the second phase of the project in Kostolac claims that the agreements are economically feasible. However, such a conclusion cannot be drawn unambiguously on the basis of the published documents. In fact, they state that raising the capacities to produce electricity is strategically important for Serbia, that it would ensure an increase in the capacity of open mine Drmno and reliable supply of the thermal power plant, that it would ensure the security of supply, reduce the import of electricity and increase revenue from VAT, employee growth in the country and the like.

Interest rates on these loans are more favorable than the one that was paid for the loans in previous years, but the list of loans that Serbia concluded in the past year also contains those with lower contractual interest rate (e.g. 2% compared to 2.5% in this agreement). A large part of the loans that Serbia has is also tied to variable parameters (e.g. LIBOR) and comparisons in this respect are not quite possible.

The explanation did not specify what would be the direct financial benefit from the realization of the project and the extent to which it would exceed the value of the approved loan with interest and additional benefits.

In order for the analysis of the loan cost-effectiveness to actually be carried out, other parameters are also required, and these parameters remained unknown in the explanation of this law. If we accepted as highly probable assumption that Serbia received a loan on favorable terms, (in regards to the interest rate and repayment period), the question remains whether these positive effects are being overrode by other contractual obligations? The agreement anticipates the engagement of companies from the creditor's country, which eliminates possible competition that could perhaps result in a more economically advantageous final tender. The agreement also stipulates that "goods, technology and services to be procured from the loan funds will be purchased mainly from China, according to the commercial contract".

In addition, the agreement anticipates the exemption from VAT and customs duties on imported equipment, which also carries a negative impact on public revenues that should be subject to consideration when determining the economic viability of the contract.

Another aspect of economic observation of the loan agreement refers to alternative solutions to the subject of procurement – e.g. how much it would cost to invest in other energy sources that could provide the same level of energy stability of the country, employment and the like. Also, one should take into account the responsibilities that Serbia assumed in connection with the important introduction of energy sources that carry less pollution, and which are not achieved by this investment. On the contrary, even further investments would be needed for "alternative sources" of energy because the volume of production of electricity from coal power plants would increase<sup>8</sup>.

Maybe such full consideration would show that the beneficial effects of this loan agreement outweigh the disadvantages. However, the problem is that these issues were not discussed in the parliament, and the explanation did not present to MPs clear calculations of advantages and disadvantages.

### **Implementation of the Law on Budget System**

Indebtedness on the basis of this credit was anticipated by the Serbian state budget for 2014 and the budget for 2015, before the law ratifying the indebtedness arrived on the National Assembly agenda. So the MPs agreed, as much as two times, that this loan would be included in the financial obligations of the Republic of Serbia even before the loan was approved!

Article 5 par. 4 of the agreement states that "the Borrower has not breached obligations under any law or agreement applied to him, which could materially and adversely affect its ability to perform its obligations under this contract, and there is also no record of failure to fulfill the obligations under this contract". However, the Borrower (state of Serbia) has clearly breached an obligation under one of its laws at the time of the conclusion of this agreement, and it continues to do so with every new loan.

The Law on Budget System, Article 27e, par. 4, p. 2) stipulates the general fiscal rule that "the general government debt, excluding liabilities for restitution, shall not exceed 45% of GDP"<sup>9</sup>. This fiscal rule has been violated long time ago, and according to current estimates, the total public debt greatly exceeds 70% of GDP. Fiscal Council, an independent body that analyzes the fiscal strategy and other documents, did not include this loan in its analysis from February 2015, since

---

<sup>8</sup> These issues and other risks due to the increased exploitation of coal (e.g. vulnerability due to natural disasters) are further discussed in the text: <http://bankwatch.org/sites/default/files/CRTAreport-Kostolac-subsidies-30Jun2014.pdf>

<sup>9</sup> [http://www.paragraf.rs/propisi/zakon\\_o\\_budzetskom\\_sistemu.html](http://www.paragraf.rs/propisi/zakon_o_budzetskom_sistemu.html)

at the time the analysis was done the loan had not yet been approved.

### **Other undertaken obligations**

The undertaken obligations seem reasonable in terms of guaranteeing the protection of interests of partners, primarily the lenders, from the occurrence of circumstances that would lead to the failure to pay the loan debt. The confirmation of stronger position of the creditor is also reflected in contracting rules of the People's Republic of China as authoritative, and the arbitration of the China International Economic and Trade Arbitration Commission (CIETAC), based in Beijing, whose decision would be final and binding for both parties.

### **The availability of information**

The provision 8.7. stipulates that Serbia will "keep all the conditions and the agreed fees in this agreement or in connection with it strictly confidential". "Without the prior written consent of the Lender, the Borrower shall not disclose any information under this agreement or in connection with this agreement to a third party, unless required by applicable law."

Although this provision stipulates restrictive regime of the access to information, it did not exclude the application of domestic legislation. On the contrary, the agreement establishes that, in cases required by "applicable law", the information will be available to the public. In our case, it is the Law on Free Access to Information of Public Importance. On the basis of this Law, any information which is owned by EPS, the company TKK and the ministries, is subject to possible requests for access to information. These requests should not be rejected automatically, because of the confidentiality clause in the contract, but only if the statutory requirements of Article 9 were met, and even then only if such a measure is necessary in a democratic society for the protection of an overriding interest. In case of request rejection, the petitioner has the right to appeal to the Commissioner for Information of Public Importance and Personal Data Protection whose decision on the matter would be final.

### **State aid**

The case of guarantees for PE Kostolac was pointed out by portal "Istinomer"<sup>10</sup> In December 2011, the Serbian Government gave the company "Kostolac" state support when it signed a loan agreement with the Chinese Export-Import Bank in the amount of 293 million dollars. This loan was taken for the revitalization of the existing blocks B1 and B2 in the thermal power plant "Kostolac", the construction of desulphurization plant, the construction of a dock on the Danube and the construction of railway infrastructure. The total value of the work at this stage is 334.63 million dollars, and the Chinese Exim Bank is financing 85 percent of the value (293 million dollars).

---

<sup>10</sup> <http://www.istinomer.rs/teme/drzavnu-pomoc-dobilo-i-privredno-društvo-kostolan/>

The Law on Ratification of the Loan Agreement for a preferential loan for the customer for the first phase of the project package "Kostolac B" between the Government of Serbia as borrower and Exim Bank as lender states that the government has obliged to return the entire 293 million dollar loan for thermal power plant "Kostolac". Under that law, the Serbian Government is the borrower and the executive government body is required to pay the Exim Bank or the lender the entire withdrawn and outstanding loan principal amount, the entire accrued interest and all obligations that the borrower is paying in accordance with the terms of this agreement. Furthermore, the law states that the PE "Elektroprivreda Srbije" is the purchaser and the PE thermal power plant "Kostolac" is the ultimate borrower. In this case, the state guarantees for the entire debt; there were no fulfilled conditions for the guarantee not to be considered state aid, but the Commission for state aid control did not consider this state aid.

The Serbian government decided to guarantee for the loan needed for the second phase of the project package "Kostolac B". In November 2013, the Ministry of Energy, Development and Environmental Protection signed a contract with the Chinese corporation CMEC (China Machinery Engineering Corporation) on the construction of the third block of the thermal power plant "Kostolac B" of 350 megawatts and the expansion of open mine "Drmno" for the annual production of 12 million tonnes of coal.

The second phase of the project package "Kostolac B" is financed from a new loan of Chinese "Eksim" bank in the amount of 609 million dollars. The entire project is expected to cost 715 million dollars, and Exim Bank is financing 85 percent, while the rest must be provided by the Government of Serbia. For this project, the Government of Serbia has allocated two guarantees. They were voted in the National Assembly in January 2015.<sup>11</sup> The end user is PE "Kostolac", the purchaser is "EPS", and the guarantees for the entire loan amount are provided by the state. The website of the Commission for state aid control contains no information that this state aid was ever discussed.

### **Cost – effectiveness study**

In order to find out more about arguments that Serbian parliament, government and EPS had in mind when accepting this legal arrangement Transparency Serbia asked Serbian authorities for additional documents. Basis for the request was the claim of the Government from the explanatory not of loan ratification law: ***the financial analysis performed on the basis of cost-effectiveness Study showed that the implementation of the second phase is economically viable and cost-effective.***

However, the only document identified by relevant ministries and public enterprises was "The

---

<sup>11</sup> [http://www.parlament.gov.rs/upload/archive/files/cir/pdf/predlozi\\_zakona/37-15.pdf](http://www.parlament.gov.rs/upload/archive/files/cir/pdf/predlozi_zakona/37-15.pdf)

bankable feasibility study on construction of the new unit rated 350 mw at the location of thermal power plant Kostolac B". This study was prepared by the ME Energoprojekt in December 2013 for the EPS.

Chapter 8 of that study brings economic feasibility analyses. It was "performed with respect to the electric power system as a whole, on the basis of the perceived technical solutions, investment values and the effects of energy production increase to the electric power system of Serbia. Financial analysis was performed from the perspective of the Power Unit itself only, taking into account the before - mentioned background information".

The study further reads:

"The economic analysis firstly observed the current state of production within the electric power system of Serbia (state without the project), and then analysed the changes brought in by incorporation on the new Unit into the system (state with project). A mathematical model was used to simulate the conditions in the system, which enables to calculate the energy effects of the construction of power plants, to check and make selection of basic energy parameters of the projected hydro and thermal power plants, and also to determine the mode of operation for current and future production capacities. The main criterion for comparing variants of development /construction of electric power system is to minimize the total costs in the same. This criterion includes investments in new facilities, the operating costs of the system and the expected costs of the planned reduction in the system, i.e. the purchase costs of the missing energy. In this regard, all cost values are discounted to the same year, in order to take into account the factor of investment and spending dynamics.

Selection of the most favorable solution among the considered variants of construction of energy facilities is carried out by the so called cost-benefit analysis. This analysis compares the benefits and costs and observed effectiveness of investments with the use of dynamic methods: net present value and internal rate of return.

Economic analysis of the feasibility of construction of new B3 Unit is conducted by comparing the discounted savings and costs. In this regard, the savings imply the investments and costs incurred in the event if the Kostolac B3 Unit is not to be constructed. In this case, it would be necessary to invest some funds and to service certain costs in a different location within the electric power system. This means that if the Kostolac B3 Unit is to be constructed, the savings that are achieved are equivalent to the investments and costs of construction at another location. On the other hand, the costs of construction of Kostolac B3 Unit are defined by specified technical solutions in terms of both the investment and dynamics of costs."

...

“For the rate of 4%/year discounted value of savings is 1,654 million USD and of costs 1,258 million USD, which makes the ratio of costs and savings to be of 1.315. Total savings during the service life of the Unit are 396.5 million USD. The presented data show that, according to the made assumptions and the data used, the investments into construction of the Unit B3 are feasible.”

“Financial analysis involves assessment, analysis and evaluation of the required project inputs, the outputs to be produced and the future benefits, expressed in financial terms. The purpose of this analysis is to estimate feasibility of investments required for construction of new Unit B3. For the purpose of financial calculation, a discount rate of 4%/year has been applied. The discount rate has been calculated on the basis of mathematical model for WACC (Weighted Average Cost of Capital). It is assumed that the interest rate for bank loan does not contain inflation. The project monitoring and valorization period covers the construction period (5.5 years) plus 25 years of plant working life. It is planned that Unit B3 starts to work January, the 1st 2020.”

Investment cost is calculated to be 726 million USD (without VAT), out of which 507 million USD in equipment. This was compared with CMEC offer of 618 million USD. Together with “other costs”, the overall amount is the same one – 726.97.000 USD. “Largest investments are related to equipment supply, which makes even 70% of total investments. Participation of civil works is 19%. Pre-production expenditures include one-time loan charges and commitment fee, the costs of insurance against exchange rate risk during borrowing period and interest during constructions, which makes even 8%. Normal operation of unit shall require working assets estimated at 11.09 million USD (1.5% of total investment).”

Results obtained in the financial analysis conducted are given in the income statement, discounted cash flow and cash flow for financial planning: “**The Income statement** shows the project's revenues and expenses during the exploitation period of 25 years. In the years observed, the revenues from the sale electricity are sufficient to cover all the costs. The average unit costs of production can be determined based on data given in income statement and they represent the cost price. On the other hand the cost price represents the base to determine a selling price of electricity on the threshold. The average unit costs of electricity production for the period observed amounting to 47.92 USD/MWh. These costs vary per years primarily depending on changes in financial costs.

**Cash flow for financial planning** of project gives the overview of actual inflow and outflow of funds during the period observed and serves to evaluate project solvency. The inflows include revenues from electricity selling and financial sources, whereas the outflow involves investments, operating costs and financial liabilities. Liquidity analysis shows that project achieves cumulative net inflow amounting to 816.12 million USD. Observing the liquidity per

years, it could be seen that during the period affected the actual inflows could cover the actual outflows of project.

The essence of profitability of the project is to assess whether project's material basis has been increased or decreased when the whole lifetime of the project is taken into account, regardless of its change in individual years. Basic source of information for project's evaluation is **discounted cash flow**. This cash flow consists of cash inflow, including revenues from the sale of electricity and residual value of the project; cash outflow, including investments in the project and operating costs and net cash flow representing the difference between cash inflows and cash outflows.“

After observing the outcomes of discounted cash flow it could be concluded that construction of TPP Kostolac B Unit 3, considering its full compliance with environmental protection regulations, is entirely feasible, resulting in positive indicators of investments profitability.“

While one may agree or oppose findings from this feasibility study, the key problem is its scope. Namely, this study discussed whether it would be cost – effective to build Kostolac B Unit 3 at all, and whether it would be cost – effective to build it using current model of financing and offer of CMEC.

However, the most crucial question remained unanswered. **Neither offer of CMEC nor loan conditions were compared against alternative solutions of building and financing of the same Plant in other way.** So, even if this feasibility study was discussed in the Parliament along with the whole contract, neither MPs, nor citizens would know anything more about cost-effectiveness of this investment model.

## Public procurement experiences - pumping water and silt from the open pit

### Introduction

In the spring of 2014 Serbia was seriously affected by the floods. Among other things, floods endangered energy sector and in particular thermoelectric plants and coal mines near rivers of Kolubara and Danube. Coal mines near Kolubara were flooded with millions of square meters of the water and mud. Government officials claimed that there is significant damage for the country. The PE Kolubara used its own equipment to remove the water, but it was not enough. Public procurement took place and works on pumping the water and silt took place few months later. The information about financing of that project were controversial, in particular in terms of World Bank's role. While the procedure of public procurement was the one from the Serbian law, some government's official claimed that tender was organized as the World Bank insisted on it. The situation became more complicated after BIRN published several texts about that procurement. These texts challenged legal basis and economic ratio of the decision to organize tender and the way how contract was implemented.

Journalists also pointed out on potential ties between the wining company and people performing public function or being related to the ruling party. The reaction from the government, i.e. prime minister was rather sharp. It was actually a series of "counter – attacks", where not just journalists and their NGO, but also the EU Delegation as the one who financed their media projects were accused.

Although such publicity created good pretext to discuss the case, it also created extremely unfavourable conditions for non-biased discussions about key problems.

### Legal initiative

In a letter which was presented at the meeting of the Committee on Finance, State Budget and Control of Public Finance of the National Assembly, February 9, 2015, Transparency - Serbia analysed various issues related to public procurement of services "CJN 08/14/DUKN - Pumping silted water and silt from the open pit PD RB "Kolubara" doo - "Tamnava - Zapadno polje". This notice was presented at the Committee meeting when the reports of civil supervisors were first discussed (in ten public procurement procedures). Since Transparency Serbia was a civil supervisor in this public procurement procedure (until the conclusion of the contract), we used this opportunity to point out to the representatives of the Committee the information on

issues that were raised after the conclusion of the contract.<sup>12</sup>

As we pointed out on that occasion, the review mainly omits the questions that were subject of civilian inspection, but addresses the considerations that preceded the announcement of public procurement, as well the questions related to the implementation of public procurement contract, which were largely disputed in public and which lacked complete information. We considered that this review deserves the attention of the Committee, as we pointed out on a number of items that should be discussed, not only for the sake of presenting complete information to the public, but also to find the best solutions for similar procurement in the future. Unfortunately, in the next three months, there were no changes to the legal framework that would be relevant for future similar cases, and no complete clarification of all issues on which there were uncertainties regarding the implementation of the specific procurement procedure.

This procurement was conducted in order to eliminate one of the most damaging economic impacts of floods in May 2014. Opencast mining of mine Kolubara - Lazarevac were flooded with about 187 million cubic meters of water and mud, which resulted in the suspension of coal production.

The main questions raised in connection with the procurement are: Has all possible been done in order for the purchase to be carried out sooner? Have the conditions and criteria been laid down to ensure wide competition and the selection of the most favourable bidders? Have the contractual obligations been fulfilled?

### **Identifying the need and manner of solving**

There was a clear need to conduct this procurement as soon as possible.<sup>13</sup> On the one hand, this need derived from the losses suffered by EPS due to the inability to exploit this open pit mine, and on the other hand, due to the maintenance of lasting stability of the electric power system.

The issue to which there has been no clear answer is whether it was possible to find a faster and more efficient solution than the one selected. In order to give an answer to it, it was necessary to analyse in detail all possible options, both in terms of the manner of work execution and in terms of ways of financing, and this was not entirely possible to do on the basis of available data.

Before it decided to formulate a subject of public procurement in such a way, the contracting authority (in cooperation with other state bodies) should have considered all possible relevant

---

<sup>12</sup> The entire analysis text is available at: <http://www.transparentnost.org.rs/index.php/sr/inicijative-i-analize-ts>  
Letter to the Finance Committee Reports of the civil supervisor, Transparency Serbia February 2015

<sup>13</sup> Of course, these arguments can be disputed from the standpoint of environmental protection, and related economic reasons. From the standpoint of environmental protection and health of the population claims are often made that the production of electricity from fossil fuels brings harmful consequences that outweigh the achieved benefits. That issue is not addressed in this analysis, but it is assumed that the economic interest in coal exploitation is already established.

options for solving problems (e.g. the engagement of mechanization in state bodies and other public companies to remove water, buying such machines to serve not only for this case but for other similar problems that might occur in the future, the procurement of pumping services or any other technical solution - e.g. one of the possible solutions mentioned in public was the procurement of "suction waterway dredgers", which was supported by the Association for the advancement of the mining profession and science). The analyses performed on this occasion and reached conclusions were not subject to monitoring, but it would certainly be important to know them, because they affect the answer to many questions that have been raised in public, among other things, the question of whether the acquisition was timely called and whether the corresponding tender documents were well-formulated.

## **Financing works**

Reaching the conclusion on how to proceed most effectively was followed by a decision on financing and procurement implementation. After the floods, a large portion of caused damage was repaired by donors. If there had been a willingness of some donors to immediately donate works or pumps and other means required for the implementation of works, the procurement procedure should not have been implemented at all. It is not known that this possibility existed in a particular case and to the extent required for the implementation of work.

Another version of financing is the use of public enterprises' resources or the budget (e.g. budget reserve funds with the transfer of subvention to the public enterprise) to implement the necessary procurement, after which would also be necessary, in accordance with the Law on Public Procurement, to modify the work program (financial plan) of the public enterprise and the public procurement plan. It is, in fact, a prerequisite for the commencement of a public procurement procedure under the Law.

A similar situation also exists when the procurement is implemented by means of funds that originally come from grants and loans - after the conclusion of a grant or loan, it is necessary to amend the work program (financial plan) of the public enterprise and public procurement plan.

In accordance with the Article 51 of the Law on Public Procurement "*originally planned funds for a specific public procurement cannot be increased by more than 10%, except in the case of natural disasters, accidents or extraordinary events whose occurrence does not depend on the will of the customer. **The Purchaser may amend the procurement plan in case of budget revision or amendment of the financial plan**, but so that all changes are visible in relation to the basic plan and that all changes are justified.*"

According to the information that Transparency Serbia received during the conduct of civil affairs

supervisor, the public procurement plan has been revised to include this public procurement. Since the work program of this enterprise was not published (which is, otherwise, obligation under the Law on Public Enterprises), nor the procurement plan (which is optional), it cannot be concluded with certainty when exactly this precondition for the implementation of procurement was met, i.e. whether there was a possibility for the public procurement to be called earlier. According to the report on the expert assessment of bids, "public procurement funds are planned by the annual program on amendments and supplements to the annual business programs of DP RB Kolubara doo for 2014, at the position II 11. Unused funds in the current year for the implementation of obligations under the referred procurement will be transferred, planned by the procurement plan and provided in the annual program of operations for the next year, or a decision on temporary financing".

### **In what cases would the acquisition not be carried out on the basis of the Law?**

Hypothetically, there could be three situations in which a public procurement procedure would not be implemented. The first option refers to the cases where the procurement is implemented by credit funds of an international financial institution and in accordance with the procedure of that international financial institution. Specifically, under Article 7 paragraph 1 of the Law, *"the provisions of this Law the purchaser shall not apply to: 2) conducted or funded procurements: (2) from the funds of foreign loans (borrowings) obtained from international organizations and international financial institutions, in accordance with the terms of an international contract or the special procedures of international organizations and financial institutions;"*

In the case of this public procurement, that did not happen. Although it was repeatedly mentioned that this acquisition was financed by the World Bank, it was implemented on the basis of domestic Law on public procurement, and not by the rules of this financial institution. Therefore, the claims of officials given to public, that "tender was required ..." because it was "... requested by the World Bank" are not grounded. In fact, the provisions of Public Procurement Law were applied to this procurement, instead of specific rules of the World Bank. Even if the World Bank did not request "anything", tender would be required, because our Law requires it, and the conditions for non-compliance with the Law were not met<sup>14</sup>.

If these statements are understood as if the funding from the World Bank contained a condition to organize a bidder tender procedure, instead of assigning a job by direct agreement, it remains unclear why would that be relevant to this particular case. According to available data, the Government of Serbia (Minister of Finance) concluded the financing agreement with the World Bank only on October 10, 2014, therefore, a few months after the procurement procedure has already started. That is the situation according to the facts and "papers". Of course, in practice it is

---

<sup>14</sup><http://www.worldbank.org/en/news/press-release/2014/10/10/world-bank-and-serbia-sign-floods-emergency-recovery-project-loan-agreement>

quite possible, and even likely, that the negotiations on the loan were conducted in parallel with the preparation of the procurement procedure, but that is of no legal significance.

Another possible case when public procurement is not implemented in accordance with domestic Law would exist in the event that the procurement procedure is regulated on the basis of international agreements (Article 7, paragraph 1.1.2.), subclause (2). For example, it would be a situation in which Serbia has concluded an agreement with another state for mutual assistance in case of natural disasters (or, for example, energetics), so that, when such a situation occurs, the agreement is activated and the company or some of the services from that country receive the job without bidding. That obviously did not happen in the case of this procurement.

A third possible case would be the implementation of the procurement without the application of Public Procurement Law, according to the following provisions of Article 7 paragraph 1: *The provisions of this Act purchasers shall not apply to (purchases): 3) to ensure basic living conditions in the case of natural disasters or technical - technological accidents whose consequences threaten the life or health of humans or the environment, in accordance with regulations governing the protection of such natural disasters;*

In all cases of such (exempted) procurements, the contracting authorities are obliged "to act in accordance with the principles of this Law" (paragraph 2). It is doubtful which other norms are applicable, except those that are explicitly listed under several articles on the principles. Transparency Serbia has already pointed out this issue to all relevant institutions in a separate document. In this document we analysed the question of possibility of applying a section of the Procurement Law that regulates the fight against corruption and conflict of interest in cases when public procurements are conducted by different rules, and not by Law, on the basis of Article 7.

15

Purchasers are usually obliged to submit their procurement plans to the Public Procurement Office (and State Audit Institution). If the Public Procurement Office determines (based on the data from the submitted plans or other submitted documents) that there are no conditions for the exemption from the Law application, it shall notify the contracting authority on that subject. Purchaser also submits to the Office a special report on implementation of such procurement.

According to media reports,<sup>16</sup> "after the floods there was a fierce debate among the management of this public company about whether to immediately proceed with the pumping of water or call a tender", "so that EPS would likely receive approval" (note: this refers to the approval of the Public Procurement Office for the implementation of the procedure under Article 7), "but that such a request was not submitted."

---

<sup>15</sup> [http://www.transparentnost.org.rs/images/dokumenti\\_uz\\_vesti/misljenje\\_i\\_inicijativa\\_za\\_dopunu\\_zakona\\_izuzete\\_nabavke\\_sukob\\_interesa\\_April](http://www.transparentnost.org.rs/images/dokumenti_uz_vesti/misljenje_i_inicijativa_za_dopunu_zakona_izuzete_nabavke_sukob_interesa_April)

<sup>16</sup> <http://www.vreme.com/cms/view.php?id=12591902015.doc>

Without going into the question whether the Public Procurement Office would have any objections to the legality of the procurement procedure under Article 7 instead of applying some of the procedures of the Public Procurement Law, we believe that such a thing would not be in accordance with the Law. The exception provides that the Law, according to this exception, does not apply when the two cumulative conditions are met. The existence of the first condition is clear - there was a natural disaster whose consequences threaten the environment. The second condition which also has to be fulfilled is debatable. In fact, it is a question of whether the removal of water from "Tamnava - Zapadno polje" is necessary "to ensure basic living conditions".

For example, this condition was undoubtedly met in situations where accommodation and food were provided for the people who escaped from the flooded Obrenovac and other places. It would be fulfilled even if, by any chance, Elektroprivreda Srbije had to introduce severe restrictions on supplies of electricity to households, as a result of the inability to use resources from the flooded areas. Therefore, the possibility to apply this exception to the general regime of public procurement should not depend either on the will of the EPS (to request its application), or on the legal opinion of the Public Procurement Office, but on an expert assessment of the factual situation - whether it is possible to provide basic living conditions for the population (the use of electricity) in another way or not?

It is obvious that the EPS concluded that this was possible, opting for a public procurement procedure, and it can be said that the later developments showed that it was possible to supply electricity to customers from other sources in the country and abroad (i.e. the fact that there were no restrictions). On the other hand, the damage caused by the inability to exploit mine Fiscal Council is described in the analysis published on July 2014 in the following way, indicating some elements that could support a different decision<sup>17</sup>:

*Although lower production of electricity during the summer months does not pose a problem, there are numerous risks that could threaten the stability and sustainability of the domestic energy system during the upcoming winter. First estimates show that the immediate environment has no significant surplus of electricity, which can complicate the planned import and negatively affect the price of imported electricity - thereby increasing EPS losses. The gas crisis caused by the possible escalation of the conflict in Ukraine, as well as the possible lack of coal in the market for household consumption, represent an additional risk to the sustainability of the energy system as, in this case, the pressure on the consumption of electricity would increase, and there is already a shortage.*

### **The application of the special Law?**

In any case, when considering important question "could the pumping start earlier" (i.e. could be

---

<sup>17</sup> [http://fiskalnisaivet.rs/images/izvestaii/analiza\\_drzavnih\\_preduzeca-fiskalni\\_aspekt.pdf](http://fiskalnisaivet.rs/images/izvestaii/analiza_drzavnih_preduzeca-fiskalni_aspekt.pdf)

intensified earlier, given that the EPS uses only the available resources), all the above-mentioned should be taken into account, as well as the need to explore the market and to define other possible conditions (e.g. drainage, environmental protection). In any case, the EPS should present convincing evidence as to whether the preparatory work was carried out as fast as possible.

Given that this provision is in connection with the reconstruction after the May floods and that the special Law was passed to, among other things, regulate procurements in order to eliminate the consequences of floods, it is important to note that the procurement procedure was initiated one day after the entry of this special Law into force (the Law came into force on July 22, 2014, and public procurement was called on July 23, 2014). Hypothetically, if a regulation (state plan) that regulates this area had been reached immediately after the entry into force of the special Law, the Law would have allowed the use of slightly shorter deadlines for implementing this purchase (10 instead of 15 days for the submission of bids).

### **Possible solutions**

The case of "Kolubara" revealed some possible shortcomings in the system of public procurement, which could be responded to by means of legislative intervention.

By all means, in this case the Purchaser suffered damage which exceeds the value of the actual public procurement that was conducted for the purpose of the damage elimination. According to some estimates from the EPS (that are probably overestimated), the damage amounted to around one million euros per day, and the total value of the work that was contracted with external partners was about 15 million euros. If these estimates are accurate, 15 days for the implementation of procurement procedures would cost as much as the entire acquisition. Even if in a particular case the estimate is not accurate or complete, it is obvious that such a case could occur in conjunction with another acquisition.

Therefore, from the standpoint of cost-effective handling of public resources, which is one of the principles of the Law on Public Procurement, there are the reasons to procure as soon as possible, even in situations where this may result in paying slightly higher price to the supplier. It is important to note that such situations may also occur when purchases are not caused by damage from natural disasters, but by some other reasons, for example, when it is known that the price of some goods would significantly increase during the time needed to prepare and implement public procurement procedure. However, the Public Procurement Law contains no provision that the Purchaser who wishes to make the best use of public resources could refer to. Of course, with the possible implementation of such exception, the legislators would have to act cautiously in order to reduce abuse to the minimum possible extent.

Another potential solution for these and similar cases that is currently not allowed by the Public Procurement Law would be the possibility to hire more contractors, and not just one. It depends on each case if something like that would be justified. For example, if one company, with all available capacities, can pump 30 units of water per day from the lake, and it is technically possible to take a total of 50 units per day in the water stream, then it would be right, in the situations when the country is suffering extensive damage due to floods, to engage all other potential contractors, and not just those who gave the best offer.

In formulating specific norm the following model could be used as a starting point:

*Deviation from the rules in the economic interest of the Purchaser*

When the contracting authority suffers material damage that should be rectified by the implementation of public procurement and when it assesses that the level of damage that is likely to occur during the implementation of the public procurement procedure would be at least twice the estimated value of the actual public procurement, the procurement needs to be implemented in the most efficient way, without performing the procedure procurement under this Law.

The Purchaser from the paragraph 1 is obliged to publish his decision and concluded contracts on the Public Procurement Portal and on his website, and to act in accordance with the principles of this Law.

The Purchaser shall notify the Public Procurement Office and the State Audit Institution about the procurements from paragraph 1 of this Article.

## **Epilogue**

The Parliament of Serbia, in August of 2015 adopted a set of amendments to the Public procurement law, partly inspired by Transparency Serbia proposals. Among other things, amendments provide much detailed rules for public procurements related to the removal of natural disasters' consequences. Even more important, this regulation is now part of the systemic Public procurement law, and not just *ad hoc* legislation.

## Belgrade Waterfront - (media) genesis of the case

For ambitious expansion plan "Belgrade Waterfront", the project (as originally announced) worth about 3 billion euros (although the investments of \$3.1 billion was also mentioned, as well as the market value of the built space of about 8 billion euros) the contracts was signed on April 26, 2015 and published only in September 2015.

Transparency Serbia limited the analysis of this project to the question of law application, transparency, handling of public resources in areas related to public-private partnerships and potential corruption risks. We did not comprise the issues of feasibility of the entire project, the urban and architectural solutions, as well as the issues of urban plans<sup>18</sup>:

Although the reconstruction of Sava amphitheatre is the project that has been mentioned since 1980s, the context of public-private partnerships emphasizes a period since the spring of 2012, when the then deputy president of the Serbian Progressive Party and a candidate of that party for Belgrade mayor Aleksandar Vucic presented the project Belgrade Waterfront<sup>19</sup>:

In the election campaign in April 2012, Vucic stated that the project<sup>20</sup> would be implemented without indebtedness, and only with the cost of 125 million euros for municipal development, but that **"the city should keep 451 million euros from the taxes for building land"**<sup>21</sup>:

However, Vucic then claimed that there are a **large number of investors** who are interested in participation in the project, but that he cannot speak of that in more detail because everyone will have to go through tender procedure.

The next important step which, as it turned out, was significant for this case, was the signing of the

---

<sup>18</sup> There is only the General Plan of Belgrade 2021 for the area intended for the construction of Belgrade Waterfront, but there is no detailed urban plan, Regulatory Plan, The Plan of detailed regulation.

([http://www.urbel.com/default.aspx?ID=uzb\\_DetaljniPlan&LN=SRL](http://www.urbel.com/default.aspx?ID=uzb_DetaljniPlan&LN=SRL))

The General Plan for this area predicted a mandatory development of tender competition: "In the initial phase, the territory of Sava amphitheater and the part of New Belgrade city from across the river will be uniquely solved as the future city center of the highest rank, through an international competition, in order to establish a logical visual and contextual link between the public spaces areas on Belgrade and New Belgrade side, regardless of different possibilities and future independent stages of implementation and specific tenders in two parts of the future city center". Professional circles warned that Belgrade Waterfront could be built even without the adoption of plans, given that the Draft Law on planning, designing and construction, Article 176, provides that "the minister in charge of urban planning, and construction can issue a location and construction permit for buildings of importance for the Republic of Serbia, if a planning document on which the location permit is based is not issued within the period prescribed by the decision on plan preparation, and based on the plan of a higher order, the rules of the profession and in accordance with the technical regulations and standards and norms for this type of object."

<sup>19</sup> <https://www.youtube.com/watch?v=bEuIjh4WQOE>

<sup>20</sup> The project planned the elements contained in the latest version of Belgrade Waterfront - after the relocation of the railway and bus stations, while preserving important cultural facilities, the construction of new facilities, the combination of business complex, luxury hotel category, residential blocks, objects with cultural and artistic content and facilities for sport and recreation, with large green areas, as well as the buildings which "would be a symbol of Belgrade." Even at that time it was announced that the construction phase and operation stage of the project would involve at least 200,000 people, that everything would be completed in eight years (the current deadline is six years), and that the total area of constructed facilities would be 1.8 million square meters, and their market value would be more than four billion euros.

<sup>21</sup> Lex specialis adopted for the purpose of expropriation for the construction of Belgrade Waterfront estimates the value of contributions for land development to 33.7 billion RSD, but allows it to be paid by means of "compensation" through the construction of public facilities.

Cooperation Agreement between the Government of the Republic of Serbia and the Government of the United Arab Emirates on February 17, 2013 and the ratification of that agreement in the National Assembly on March 15, 2013.<sup>22</sup>

The agreement,<sup>23</sup> in fact, planned the "cooperation in the field of real estate/immovable property/capacity", which includes "a) Acquisition of immovable property owned by the state, and/or b) Joint c projects involving immovable property owned by the state." The agreement further states that, in order to invest in "certain capacities and immovable property in the Republic of Serbia, which is state-owned, the Republic of Serbia agrees to sell certain real estate units to the entities in the United Arab Emirates in cases when a common interest is recognized or to make a joint investment, according to the rules and under the terms agreed between the Parties in this agreement, or each Party or the private sector, or the private sector of both Parties, which will be regulated by separate sales or other contracts."

This met the precondition for the Belgrade Waterfront to be implemented as a public-private partnership, without the application of anti-corruption mechanisms from the Law on public private partnerships and concessions, which provides transparency and competition - the preparation of a study which should explain the choice of PPP instead of some other form of project realization, then the competitive process for the selection of partners (public competition) even in the case that there is an investor with the project and offer to implement<sup>24</sup> it, the development of a business plan that includes the requirements of PPP, **cost assessment and analysis of obtained value compared to the invested funds**, specifications of financial admissibility of PPP for a public body, **specifications in terms of project funding** and the availability of funds, **the planned allocation of risk**, followed by the **analysis of economic efficiency of the proposed project**, the types and amounts of collateral provided by the partners in the project, and the mechanisms for monitoring the realization of the contract and the commitments, which includes the regular, six-month reporting. The law also precisely prescribes what needs to be included by a contract signed by a public authority (in this case the state of Serbia) and by a private investor. All of these obligations can be avoided due to the fact that the PPP is implemented on the basis of interstate agreement.<sup>25</sup>

In October 2013, the media announced the intensive work on the project implementation, or that the "experts entrusted with the project" completed the preliminary design in the past year and a half (after the 2012 elections), obtained proprietary lists for more than 400 cadastral parcels,

---

<sup>22</sup> <http://www.parliament.gov.rs/upload/archive/files/cir/pdf/zakoni/2013/817-13.pdf>

<sup>23</sup> Article 2, Paragraph 8

<sup>24</sup> Article 19 of the Law on PPP and Concessions. Within 90 days of receipt of the specific voluntarily proposal, the public body determines whether it considers the project to be of public interest and in that sense informs proposer. If it is considered that the voluntarily proposal is of public interest and if the public body decides to initiate the project, the body further initiates a regular procedure for the selection of private partner and the award of contracts, in which the bidder is entitled to participate provided that "his participation in the preparation of project proposals does not affect competition".

<sup>25</sup> TS repeatedly (including the work on anti-corruption strategy) indicated that the area of investment in major infrastructure projects on the basis of bilateral agreements is one of the most problematic issues from the standpoint of the fight against corruption, but it was never included in the final text of the Anti-corruption Strategy.

obtained "all necessary requirements of public companies and other competent institutions for the relocation of traffic and communal infrastructure" and that "the development of a plan of special purpose areas is in progress and that it will be submitted for approval in January 2014".

Srdjan Rugar, who was presented as a "team leader, who is in charge of the project and a future director of "Company Belgrade Waterfront" said to "Novosti" that "Belgrade Waterfront" gained the status of project of special importance for the Republic and that the "foreign investors, companies and investment funds, recognized it as a realistic and cost-effective."

"At the request of the Government of Serbia, the Ministry of Economy will form the company 'Belgrade Waterfront' and that part of the work is in its final stage. After obtaining locations, all investors will become part of the company by means of recapitalization and, of course, will build at their own expense. For this project, Serbia will not borrow a single euro of loan". Rugar also stated: "Investors are not being deceived, but they are being sold clean locations equipped with infrastructure. By the beginning of the construction phase of the complex there is the need for the investments of around one and a half to two billion euros. "It is interesting that it was established that during the preparation of the project "special attention was paid to respecting urban demands" and that **"everything will be in accordance with the city planning documents that are in force," although the planning documents for that part of city do not exist.**

Two weeks later (E-Gate October 16, 2013) Rugar declares the aim of Serbia is to avoid a single euro debt in the realization of this project, "We want something that can and must be achieved. By means of our own funds we should create conditions **for foreign investors to 'confront' who will get the location and build at their own expense.**"

Three months later it turns out that **there is no "conflict of investors"** about who will get the location, but one investor emerges from a country with which there is a signed intergovernmental agreement on cooperation, and Aleksandar Vucic, who in 2012 announced that all interested in participation in the project **will have to go through the tender procedure**, now says that the public authorities will respect the law, but that **other people's money must respect as well**, and that the person who advocates the announcement of the tender competition should first "find 3.1 billion dollars<sup>26</sup> and then announce a **competition.**"

On January 18, 2014, a businessman from the UAE Mohammed Al Abar spoke with Vucic in Belgrade about investments in the project "Belgrade Waterfront." Then the public in Serbia was informed that Al Abar presented the project "Belgrade Waterfront" to Vucic which should mean that it is a new project with the same name as a pre-election project from 2012.

---

<sup>26</sup> Eventually, it turned out that the investor would invest 150 million euros of his own money.

Interim President of Belgrade Sinisa Mali said at the time that the company Belgrade Waterfront would be established as soon as possible and the expropriation of the land not owned by the Republic of Serbia was initiated, and he added that at the same time planning documents would be prepared so that the first development phase of the project could begin in late 2014.

Given that the legal nature of the business was not mentioned and the explanation of what happened to the announced public competition was not given, in a statement from the following day Transparency Serbia asked the question "What is "Belgrade Waterfront?" - Is it a project that is intended to ultimately be financed by taxpayers, by repaying the loans for conducted procurements? Or is it the sale of state land to a foreign investor who will then on its own account and risk try to sell or rent the properties? Or is it a public-private partnership, where the joint company between Serbia/City of Belgrade? and the company whose owner presented the project will build, sell and lease commercial space and apartments.

In relation to that, Transparency Serbia asked the following questions:

*1. Did the Republic of Serbia/ City of Belgrade give the opportunity (e.g. called the tender) to other potential investors to form a joint company and provide the project for the construction of "Belgrade Waterfront"? If not, on the basis of which regulations was the competition excluded?*

*2. Does this mean that in any future case when a potential investor presents a project that plans the formation of a joint company in which the state/city will invest their land and the investor money, the state/city would accept such an offer or the country/city will act selectively towards investors?*

*3. How will the investments, profit and business risk be divided in the future "joint company"?*

*4. What is the legal basis for the formation of the joint company, is it a project of public-private partnerships, was it defined by the Commission for PPP, as provided by the Act of 2011?*

On the same day, the President of the Association of Architects of Serbia, Igor Maric said that a solution for regulating the part of Belgrade along Sava River should be selected during an international competition, instead of a big project Belgrade Waterfront being built on *ad hoc* basis.

Aleksandar Vucic replied "that the public authorities will **respect the law**, but that **people's money must be respected as well**, and when asked why there was no tender competition for the project, he said he wouldn't mind that, but he would like for the representative of the association of architects who sought to announce a competition, "to find 3.1 billion dollars, and then to call a **competition**."

The following day, Transparency received a reply from the president and secretary of the Interim organ of Belgrade Sinisa Mali and Goran Vesic. Vesic said that the project would be implemented in full accordance with the law, **but there was no obligation to announce a public competition.**

However, Vesic and Mali presented a series of trivial or even meaningless scores and statements, like the one that the mentioned project is "in constant tender competition around the world for several decades and that no one has ever applied except one company from the United Arab Emirates" and that "during the last 20 years there have been intense talks about the project Belgrade Waterfront and that so far no one applied." Mali even called "all people from Transparency Serbia to speak out if they know any interested investors" and "they" will provide the project.

After this, Transparency Serbia repeated the question about the nature of the legal work that the authorities of the Republic of Serbia and/or the City of Belgrade intend to undertake with a company from the UAE<sup>27</sup>. To this Sinisa Mali replied that the Republic of Serbia will implement the process in connection with the project "Belgrade Waterfront" in accordance with the laws and added that "when this happens, everyone, including the organization Transparency Serbia, will be able to assess this procedure and determine whether it was conducted in accordance with the law".

It is obvious that at this stage and in the election campaign, the authorities did not want to openly announce that **nothing specific has been signed**, nor to communicate the planned PPP, which was exempted from the application of the Law on PPP, thanks to the interstate agreement with the UAE.

As Sinisa Mali said, instead of a public competition prescribed by the law, in recent decades we had several projects that dealt with the descent of Belgrade to Sava River. According to the

<sup>27</sup> In addition, there was the repeated information that we had also heard before - the total area of "Belgrade Waterfront", including residential and commercial property, will amount to 1,850,000 square meters. The length of the boulevard will amount to 1.8 km with the width of 40 meters. The project will be built in three major phases, and the first phase will have five stages. The first ones are the Tower of Belgrade and the shopping center. This time there was no mention about the 200,000 people who will be employed during construction and exploitation, but rather about "the inclusion of Belgrade firms and architects during the construction" and the employment of around 20,000 people.

As we have pointed out, these construction projects can basically be implemented in several ways: 1) City/Republic can finance the construction of buildings and regulation of land from the budget, or credits, and to organize public procurements for the purpose of implementation of the work; 2) City/Republic can sell the land to one or more interested investors; 3) to conclude some form of agreement on public-private partnership (concession, the formation of a joint company with joint investments and the like). To each of these forms of business special laws of the Republic of Serbia are applied (Public Procurement Law, the Law on Public Property or the Law on Public - Private Partnership), and the rules relating to the urban and spatial planning are applied in any case.

If public-private partnership was already agreed (the formation of a joint company), as it could be inferred from the previous statements of Mr. Mali, we pointed out that it is necessary to present the public with information relating to the current and future implementation of the current Law on public-private partnerships, especially in relation to competition, non-selective conduct of authorities, the protection of public interest (the division of investment and business risk in the joint company) and the implementation of the procedure prior to the conclusion of such an arrangement.

Because of all of the above-mentioned, it is completely obvious that the fact that "the project Belgrade Waterfront has been the subject of discussion for 20 years" in no case provides answers to the questions raised about the implementation of regulations of the Republic of Serbia on this legal work. Also, given that the association Transparency - Serbia is devoted to the fight against corruption and transparent work of public bodies, and that it has never dealt with search for investors or with establishing the quality of potential investors (including the company Eagle Hills), we consider the comment of Mr. Mali as inappropriate.

interpretation of Sinisa Mali, those decades were "an open public invitation" to which one investor finally applied and decided to invest several billion euros.

In the following weeks, Belgrade Waterfront was the election issue. Little could be heard about the legal nature of the work, about the obligations that would be accepted by the state, and even less about the costs of "preparing the ground" for the construction.

Through the media, citizens were informed by Sinisa Mali on February 5, 2014, about the **"proposal that we would invest the land, that the Arab investors would invest the money and that the profit from achieved investments would be shared according to a certain percentage.** This percentage is currently being negotiated and it will soon be known and agreed. The question who will invest the supporting structure on the land remains, but that is the subject of ongoing negotiations with investors from the UAE."

General plan for the construction of the project "Belgrade Waterfront" was presented on March 2, 2014 in Dubai, when the preliminary designs for the Tower of Belgrade and the shopping centre were also presented. All of this was presented by Mohammed Al Abar, a potential investor or director of the newly established company "Eagle Hills", which is the announced project investor.

We found out from the announcement of the Government of Serbia that the company "Eagle Hills" has already announced a tender competition for architectural solutions for facilities - the Tower of Belgrade and shopping centre, and that the competition "involved the most famous companies in the world, including the American studio 'SOM', which is the maker of the tallest buildings in the world - Burj Khalifa in Dubai:<sup>28</sup>"Four international companies have already submitted eight proposals for the Tower of Belgrade, four of which entered the second round, while two proposals for the shopping mall entered the second round.

Only a few days later we found out that the contract with the investor was not signed, but without the explanation of how it is possible for an investor to announce a competition for the construction of buildings in Belgrade Waterfront before signing the contract (or before the public announcement that the contract was signed).

Upon his return from Dubai, Sinisa Mali said that the entire project would be financed by a partner from the United Arab Emirates, and our costs will be bringing infrastructure to the location. "It actually already exists and we do not expect excessive costs, except the cost of expropriation and resettlement."

---

<sup>28</sup>In addition, there was the repeated information that we had also heard before - the total area of "Belgrade Waterfront", including residential and commercial property, will amount to 1,850,000 square meters. The length of the boulevard will amount to 1.8 km with the width of 40 meters. The project will be built in three major phases, and the first phase will have five stages. The first ones are the Tower of Belgrade and the shopping center. This time there was no mention about the 200,000 people who will be employed during construction and exploitation, but rather about "the inclusion of Belgrade firms and architects during the construction" and the employment of around 20,000 people.

This was followed by the announcement about the beginning of reconstruction of the building "Geozaovod" in Karadjordjeva 48, which will be "the centre of all events in connection with the project "Belgrade Waterfront". By the decision of the Government the building was assigned to the Ombudsman, but this state body did not move in because the building needed renovation, for which there was no money in the budget. Through the media, the Ombudsman found out that the intended purpose of the building was changed in practice although the Government has not adopted a new decision that would change the user of this property.

As it was said, two million euros for the reconstruction of the building was provided by a company from the UAE. It was announced that this money was received in the form of donation. This also happened before any contract for the project Belgrade Waterfront was signed (or at least before the public announcement that the contract was signed).

Among the legal details that are scarcely revealed, there is also the information that "property-legal relations for this area<sup>29</sup> are legitimate, the land is owned by the Republic of Serbia, and the user is 'Railways', and when the company "Belgrade Waterfront" is formed as a property of the Republic, then the entire land in question will be attributed to this company and conditions for expropriation will be created."

Finally, on March 5, 2014. Sinisa Mali revealed that the contract has not been signed but that Serbia was "very close" to signing the contract with investors from the United Arab Emirates for the project "Belgrade Waterfront" and two days later that the contract will be signed after the formation of the new government, which reveals the message that the government stands behind this project.

Then we found out that most of the elements of the contract were already agreed upon and that the division of profits is not yet defined and is still in progress.

Sinisa Mali also announced the estimates that cleaning of Sava amphitheatre will cost "tens of millions of euros", which be multiply reimbursed to Serbia. Clearing the railway tracks and rails, which is the first phase in the cleaning of Sava amphitheatre, will cost 2.5 million euros and will be financed by the Government of Serbia. And only after the expropriation process, that will happen after the establishment of "Belgrade Waterfront" company and after the Tax Administration conducts the assessment, we will know the total cost of the cleaning of Sava amphitheatre.

Mali further revealed certain amounts related to other investments linked with Belgrade Waterfront - the completion of the ring road will cost 250 million euros, the completion of the railway station Prokop 20 million euros, while the price of relocation and construction of the railway station will be known two months later upon the completion of preliminary design. It was

<sup>29</sup> Applies to the area planned for the first phase of construction.

not stated what sources will be used for this funding.

Finally, a day after the elections, on March 17, 2014, the coordinator of the project "Belgrade Waterfront" Aleksandar Karlovcan declared that the master plan of the project (which was launched in Dubai) will be presented to the public the following month.

In the following period, the city authorities adapt spatial plans to the needs of investors and politicians announce the start of construction for spring 2015<sup>30</sup> and for the period "until the end of the summer 2015"<sup>31</sup>.

At the meeting on May 1, 2014, the Government of Serbia adopted a "conclusion according to which the Project for regulating the coastal area of Belgrade - "Belgrade Waterfront" was determined as a project of importance for the Republic of Serbia". Transparency Serbia then pointed out to curiosity - in contrast to other acts which were adopted at the same Government meeting, that conclusion has not been published on the web page [http://www.srbija.gov.rs/vesti/dokumenti\\_pregled.php?id=208905](http://www.srbija.gov.rs/vesti/dokumenti_pregled.php?id=208905)

Government conclusions are usually not published, unless the government itself decides otherwise, but it was illustrative that we learned from the Government meeting statement that this project, worth several billion euros, exists as a shaped document, and this was revealed only in a form of a statement and without any further<sup>32</sup> details.

This was followed by a change in the General urban plan: General urban plan should present a strategic urban vision of the city development, which is the product of a serious work of experts and to which investors will adjust. Given that we had the opportunity to hear from the Prime Minister that Serbia must obey the law, but it must also respect "someone else's money", it is not surprising that the General urban plan is being changed to better suit an investor.

In June 2014, the website of the city of Belgrade<sup>32</sup> announced the beginning of "public inspection" into the amendments of General urban plan, which were planned to last until July 9. The purpose of this ad was only to meet the form of the Law on planning and construction.

The essence was recorded in one sentence of the proposed amendments: "If the Government of the Republic of Serbia identifies any of the aforementioned locations as a location of importance for the Republic of Serbia, such a location does not require a tender competition". On May 1, 2014 the Government determined that the project Belgrade Waterfront is of importance for the Republic of Serbia and that conclusion presents an annex to GUP draft amendments.

---

<sup>30</sup> <http://www.blic.rs/Vesti/Ekonomija/502061/Beograd-na-vodi-pocinje-da-se-gradi-na-prolece-2015>

<sup>31</sup> <http://www.blic.rs/Vesti/Beograd/548639/Do-kraja-leta-mogli-bi-da-pocnu-radovi-u-okviru-Beograda-na-vodi>

<sup>32</sup> <http://www.beograd.rs/cms/view.php?id=1606936>

What did the changes bring? When Belgrade Waterfront was presented, urban planners pointed out that this project envisions the regulation of only one bank, although GUP envisions that "the territory of Sava amphitheatre and part of New Belgrade city from across the river are uniquely addressed in the initial phase as a future city centre of the highest rank, through an international competition and in order to establish a logical visual and contextual link between public areas on Belgrade and New Belgrade side, regardless of the different opportunities and future independent implementation phase and specific vacancies in two parts of the future centre. The area of public open space on both sides (streets, squares, parks, quays) is about 50% of the entire territory. The area on both banks is aimed at business and exclusive apartment, with a surface area ratio of 1:1". The problem is solved - this paragraph is deleted from the proposed GUP changes.

One of the reasons for changes is "the Tower of Belgrade", or (investors') plan to construct a building in Sava amphitheatre with a height not previously allowed by the plan. This is now possible because in April the Interim body adopted a Decision on the termination of Study on high buildings of Belgrade.

There is an interesting aspect of consultancy of changes in the process. Urban plans are acts for which the law requires public hearing or public display. What was that like in the case of Belgrade GUP? From the means for the realization of public insight, the city administration predicted personal appearance in the basement premises of city administration at the address 27 Mart, on weekdays from 9 am to 6 pm. The proposal to amend the plan was not posted on the website of the City of Belgrade with the news. When a site visitor clicks on the box "General urban plan of Belgrade 2021", he could conclude that there are no changes in progress.

Modern means of the 19th century were provided to receive objections to the planned solutions for the 21st century - the submission through the registration office.

Transparency Serbia prepared and submitted specific objections<sup>33</sup> to the "Draft amendments to the General Plan of Belgrade 2021". Most of the objections were of general nature - non-disclosure of acts to which the draft refers (e.g. The conclusion of the Government in connection with the project "Belgrade Waterfront"), lack of explanation of how the proposed changes will better meet the needs of the state and the city, anachronistic way of discussion (inability to submit remarks by e-mail) as well as undermining the debate before it even started - the publication of information that the project "Belgrade Waterfront" would be implemented (which is not in accordance with the actual urban plan), due to which it can happen that the current "public access" is merely satisfying form of the Law on planning and building, and not a chance to resolve all important urban issues.

<sup>33</sup> <http://www.transparentnost.org.rs/images/stories/materijali/25062014/primedbe%20TS%20javni%20uvid%20izmena%20i%20dopuna%20Generalnog%20plana%20Beograda%202021%20jun%202014.pdf>

Specific complaints referred to those changes that may pose a risk from the standpoint of the appearance of corruption or which have not been properly explained. The first such change is the abolition of the international competition for the design planning of "Sava Amphitheatre" and the second is the introduction of opportunities to use lower planning documents and projects to deviate from the established maximum height and number of building storeys (all remarks are available on Transparency Serbia website).

Public meeting of the Commission for the plans of Belgrade City Assembly was held on July 22, 2014 when our objections were rejected.

Members of the Commission declared<sup>34</sup> that they have no jurisdiction to provide an answer to the question why GUP is being changed, but they named the initiators of changes as responsible for the overall legal framework - currently non-existent Interim legal Belgrade body that made the decision to change the plan. The Commission declared itself incompetent to the appeal of the Directorate of waterways in regards to the decision to build a low bridge across Sava, which would make this international navigable river no longer navigable, and the state of Serbia would thus violate international agreement on the navigation along Sava. The same thing happened with the appeal to preserve the appearance of the building of the main railway station, while the appeal for the abolition of joint regulation of both banks of Sava was addressed by the explanation that the amendments to the plan do not apply to New Belgrade.

Upon our indication to the lack of supporting documents, such as the Resolution of the Government on the regulation of coastal areas to which the Urban Institute referred in the proposed amendments (this Government's conclusion is not possible to find in the documentation, or on the sites of the Government of Serbia, Belgrade and the Urban Institute), the Commission established that this conclusion does not exist and continued its work.

**In September 2014, the amendments to urban plan were adopted**, which Transparency Serbia called "the victory of the investor urbanism": "General Plan of Belgrade 2021. was amended on September 19, 2014 by the decision of the Belgrade City Assembly. A number of plans for detailed regulation were also amended. As stated in the news on the City website, "the reason for the amendment was a need to revise the rules of plan implementation, i.e. the obligation of calling tender competition and public professional inspections for individual locations, then the possibility for the construction of high rise buildings on the entire territory of the city and the planned purposes of the territory of Sava amphitheatre, particularly in terms of relocation of rail transportation". The bottom line is expressed at the end - all amendments to the plans are related to the" infrastructure that should support the project "Belgrade Waterfront".

The meeting report on the City website does not mention any actions of dissatisfied citizens who

<sup>34</sup> <http://www.istinomer.rs/stav/analize/zakljucka-nema-a-gup-se-menja/>

briefly interrupted the session. Public debate, that is, public review of these project changes was eventually reduced to meeting the form, because the essential decision was already reached elsewhere and it was impossible to change any part of the proposal which would affect the realization of the project "BG Waterfront" in a predetermined manner.

The response of the Belgrade City Administration - Secretariat for Urban Planning, states that our "general remarks are not grounded". Our first general objection referred to disclosure of related documents - the decision on amending the General plan and the Conclusion of the Government on establishing the Project "BG Waterfront." The Secretariat responded that the decision on making amendments to the plan was published in the Official Journal of Belgrade (at the time of documenting the objections we did not manage to find it there) and that "the integral part of that decision is the explanation" (the explanation has not yet been published). The Secretariat does not address the non-publication of the Government conclusion.

The second general objection concerns the manner of publication that it was supposed to be allowed to electronically submit comments. The third general objection addresses the purpose of undermining public inspection - the fact that the highest officials of the state and the city have repeatedly announced the implementation of the project and the dynamics of the job, that they have started business relations with prospective investor and that redesigning the plan is the precondition for the project to be implemented, and that **the debate on amending the plan and allowing the submissions of objections has no sense if the decision is made in advance**. Secretariat provided no response to this remark.

The fourth general objection refers to the lack of explanation about the reasons (e.g. how the proposed changes better satisfy the needs of the Republic, City and City municipalities"). This response was not provided as well, unless it is contained in the unpublished explanation.

When it comes to specific comments, the Secretariat "partially accepted" objection to the abolition of the required international competition for the regulation of Sava amphitheatre. However, instead of explicit revocation of the competition implementation, this was performed indirectly, by saying that " the need for holding competitions will be re-examined", which will obviously lead to the same outcome: the officials of city secretariat and expert committee would "re-examine" the need for organizing an architectural competition, a few months after their superiors began to be photographed next to the completed models of the future appearance of that location and after the city TV station made special show dedicated to this project!

The Secretariat refused the remark that applies to legally impossible amendment of the General plan - amendment of non-existing Articles. What actually happened? The City website contains a large banner that leads to the text of the General plan, but it turned out that this is not a valid

version of this document!"

Soon afterwards it was disclosed **how the foreign investor affected the changes of urban plans**. In early October, in an interview with "Politika", director of the Planning Institute of Belgrade Nebojsa Stefanovic, in regards to the detailed regulation plan for a part of Sava district that is currently under so-called "public inspection", said many interesting things. In what appears to be an attempt to convince us that all the regulations have been met and that we will get "a more beautiful and older" district, he, in fact, disclosed a series of information that reveal everything that has been adapted to the investor who made a deal with politicians. Information that we were able to read cause serious worry:

1. "It is better to allow high buildings on the right bank of Sava, instead of having devastated area as Sava amphitheatre is now ". This assessment certainly sounds reasonable. But it is not true that "the devastated area" and "high buildings" were only options. Before the recent amendment, the General plan of Belgrade anticipated mandatory international tender for the regulation of this location which could envision whatever profession believed as best. "High buildings" are just a wish of one interested investor (a public invitation to other interested parties to apply was never opened), and the urban plan was (partly) adapted to these wishes.

2. "Allowing Arab investor "Eagle Hills" to build a shopping centre in the extension of Visegradska street and a residential complex near the old Sava bridge was one in a series of compromises accepted by the team of 111 engineers from the Institute". In other words, the Institute considers this a poor solution, but they proposed it because it is the desire of the investor, and of the specific company that has not yet concluded a contract for the sale or lease of the land, but with which "negotiates" what will be built.

3. "Urban planners resisted the pressure from investors to approve the highest possible density of the complex, which would result in more square meters and profit but the life in such a complex would be less pleasant. Instead, the Institute instructed the company of Mohammed Alabaré that the first business object has to be at a distance of 110 meters from the Tower, and the first housing object cannot be "build closer" than 146 meters. "In addition to what has been mentioned, here we learned that the investor made pressures for the urban plan to be composed in a specific way. It is certainly interesting to think about the economic calculation - that the investor has an interest to make as many "square meters" as possible, but in this case they would lead to a "poor quality of life" (and therefore a lower cost per "square meter").

4. "Investor was surprised about everything that must remain a public property. We banned construction over three collectors that collect rainwater from Sava slopes and discharge it into the river." Under the normal circumstances, investors should not be surprised by anything related

to urban plans. Under normal circumstances, investors would come only after General plans are already made, and they would use those plans to assess whether they have interest to build in this area only what is allowed. After that and for the purpose of selling or leasing the land the investor with the best offer is selected.

5. "For the purpose of traffic connection between old city and New Belgrade we left the possibility of building tunnels in the area from Kamenicka to Francuska street, but we have to think about how to allow the transport of vehicles from the Boulevard of Zoran Djindjic, which is the most congested, to the old part of the city." Exactly, that's what needs be considered. But not later, after the project that impedes or prevents that is approved, but in advance. That is probably why the former General plan of Belgrade scheduled the joint solution of urban issues both on the left and on the right bank of river Sava.

6. "The competition was not held because that was the agreement between politicians and investor. This is a project of national importance, the investment of three billion dollars, which is very difficult to fund anywhere in the world. We modified the conceptual design of investors in accordance with our professional attitudes, the law and conditions of 75 city and state institutions." Indeed, it is not easy "to find three billion dollars" for investment. If this was a public investment, then the state and city authorities would have to come up with an idea what to build, how much it would cost, how it would be funded, and whether would it be worth at all. If this was a private investment, then the state and city authorities would open the possibility for investors to apply, offer, calculate if they have a business interest to invest money and how much they want to invest in their property. In this case neither has been done, we have an announced investment that is both "public" and "private", and without any conducted analyses or processes of the Law on public-private partnerships (which will probably be legally "covered" on the basis of interstate agreement and Government decisions) a contract between the public and private partner has not been signed, and the essential elements of the future agreement have not been made public, or at least the minimum requirements of the state in this regard (e.g. share of investment and profit, share in the business risks).

7. "Both the mayor and the investor had understanding for such corrections." It is clear why the Director of the Urban Institute said that the investor had understanding for the correction of the plan that was "presented". But it is not clear why the mayor was asked about this question in the first place. Urban planning decisions are made by the city council (an independent body in relation to the mayor). The conditions of the contract with the investor will, since it refers to a state property and to "a project of national importance," be negotiated by the Government of Serbia. If the corrections, as suggested by the director of the Urban Institute, are based on the regulated obligations, then the correction should not depend on the "understanding" of any official, even the mayor, but should pose a requirement.

We requested the Urban Institute to submit the information of public interest related to the development of the draft and Director's drafts. We requested the information on the legal basis of the use of the document titled "Belgrade Waterfront Concept Masterplan, Eagle Hills, Abu Dhabi 2014, Belgrade Waterfront Detailed Masterplan, Eagle Hills, July 2014" in preparing the document: REPORT on strategic assessment of the environmental effect of the spatial plan, the information on whether the document - "a master plan", or any other document that the Urban Institute received from any other legal or natural person, other than the competent state organs, was used in draft spatial plan.

We requested the information about the legal basis, kind of authority and the manner in which Urban Institute conducted negotiations with the investor, i.e. the information on how the investor made pressure on the Institute, as can be inferred from the text published in the daily newspaper "Politika" on October 5, or, a copy of the request for correction of statements from the text, if the information that was published in the daily newspaper "Politika" was not true. The answer to the request was not received, so we complained to the Commissioner and received the reply only after the complaint.

The response explicitly claims that the Institute has not received documents from other natural and legal persons in connection with the draft and that it does not have the "Master Plan" prepared by the company "Eagle Hills" from Abu Dhabi. However, we received no answer to the following question: - the information about legal basis, kind of authority and the manner in which Urban Institute conducted negotiations with the investor, or, the information on how the investor made pressure on the Institute, as can be inferred from the text published in the daily newspaper "Politika", or, a copy of the request for correction of statements from the text, if the information that was published in the daily newspaper "Politika" was not true.

In its response, the Urban Institute claims that we requested comments and not "public information".

However, that is not true. Namely: 1) The public authority must have the information about whether or not it sent a copy of the request for correction to the daily newspaper "Politika"; 2) The public authority must have information about legal basis, kind of authority and the manner in which it conducted negotiations with the investor, or the information that such negotiations were not conducted, that they were conducted without any legal basis or without authorization; 3) it would be reasonable to expect that the authority has the information on pressures, in case there were any, e.g. official notes about it, correspondence, minutes from the meetings and the like.

Afterwards, in October 2014, Transparency Serbia proposed the Republic agency for spatial planning and the Secretariat for urban planning and construction of Belgrade to withdraw **the**

**draft spatial plan** for Sava coastal area (project "Belgrade Waterfront") from the public debate and to start preparing a new one, because the spatial plan has been developed contrary to the regulations, with compromises with the potential investor and under the investor's pressures.

In the explanation of the proposal (integral text of remarks on our website: in a file named "Transparency Serbia objections to the plan of special purpose public review, October 2014.doc") Transparency Serbia pointed out that the draft spatial plan was made contrary to the decision on the development of spatial plan and to the acts of higher legal force, and at the same time does not contain the complete and essential information about the Plan drafting process and the documents that were used on this occasion.

By comparing the content of the Decision, the conditions that it stipulates for the development of the Spatial Plan, the content of the Spatial Draft, but also the allegations presented to the public by Director of the Urban Institute of Belgrade Nebojsa Stefanovic in the daily newspaper "Politika" on October 5, 2014, we noticed a number of omissions, irregularities and illegalities due to which it was necessary to compose a new draft.

However, it is illustrative that the Plan of special purpose area, which at that time was still in public debate, in early November won the award at the Salon of Urbanism in Belgrade. That was the reason for the presidency of Urbanist Association of Belgrade to resign.

**In January 2015, the Government of Serbia finally adopted spatial plan**, and the Republic Agency for Spatial Planning has not responded to any of the objections applicants to their remarks on the draft plan.

What actually happened to the remarks? They were supposed to be discussed in December 2014 by the Commission of the Agency for spatial planning and to submit the report with explanations about which remarks were accepted and which were supposed to be published on the institution's website. The now former director of the Agency Dragan Duncic confirmed to TV Network that the Commission prepared the report on 269 pages, but that it was never published. In fact, the agency was closed on December 17 due to the entry into force of the amendment of the Law on planning and construction. Employees, assets, property, documents and archives were taken over by the Ministry of Construction. However, TV Network failed to find an interlocutor in the Ministry who would say which objections were adopted, and which were rejected.

The adoption of the spatial plan created the conditions for the beginning of construction works, or when the plan comes into force, it will be used as a basis for issuing location and building permits. Meanwhile, in January 2015 a stand for the promotion of the project "Belgrade Waterfront" was opened. As it turned out, the stand was actually a hospitality facility. For the

construction of this facility, municipality Savski Venac last year issued a decision to the Company "Belgrade Waterfront" for temporary occupation of public space and their license is valid until July. According to media reports, this promotion consists of issuing brochures with the information about the project to "stand" visitors.

The next step was the completion of **expropriation** for the purpose of construction. It turned out that the Law on expropriation does not allow the expropriation of private property for the purpose of construction of commercial or residential commercial buildings, or the buildings intended for tourism and catering. For this reason Serbian government established and the Assembly adopted the **lex specialis**.

In fact, Serbian government established the Draft law on determining public interest and specific expropriation procedures and the issuance of building permits for the realization of the project for the construction of "Belgrade Waterfront".

This refers to the law that allows the expropriation of buildings and land in private ownership in the area of development of future residential and business centre in the coastal area of Sava, on the basis of the previously adopted "Plan of special purpose" and Government decision on designating the project "Belgrade Waterfront" as a project "of importance for the Republic of Serbia and Belgrade."

By means of this draft law, the government practically informed citizens that the Law on expropriation and the accompanying established rules would be a "dead letter" whenever the Government establishes that something is a project of national importance. As Transparency Serbia pointed out at the time, it would be more appropriate to amend the Law on expropriation by introducing new reasons that could be applied in future equally in all similar situations, and not on a case-by-case basis. For example, if the government considers that the projects in which the state provides the building land and a private investor provides the money to build a facility, and all for the purpose of further sale on the market (which is actually the case of "Belgrade Waterfront") represent the "public interest", then it should put that in writing, explain and try to justify to MPs.

The constitutionality of this law will depend on the decision of the Constitutional Court of Serbia. In the past and in some cases, this institution has taken a stance that the legal system is violated when the provisions of a special law are in conflict with the systemic law, as well as a completely opposite view (e.g. when the Court left in force the Law on assistance to the construction industry, even though it was contrary to the systemic Law on public procurement). In addition, there may be possible constitutional challenges on other grounds, for example due to the interference with the right to peaceful enjoyment of property. Generally, from the legal point of view, the main

problem in the entire story is that the expropriation may be performed "in the public interest", and the term "public interest" is not clearly defined in the Constitution.

Transparency Serbia tried to point out to MPs a number of controversial decisions in the "lex specialis", irrespective of the question of the law constitutionality<sup>35</sup>.

Among other things, it was pointed out that the Law opens up the possibility to sign a contract with an investor without a public procurement procedure and to build facilities for public use and thus "settle up" the costs for the regulation of the construction land.

These are the works worth 33 billion RSD (around 10% of the value of all public procurements in Serbia in 2014), and an interesting coincidence is that the estimated value of the regulation of the construction land is almost identical - 33.7 billion RSD.

Opening of the opportunity that the public procurement of works gets entrusted to predetermined firms, without competition, can result in harm to public funds. In the absence of competition the investor who performs such work would have an interest to show higher cost of operations, to thereby repay more contribution for the construction land.

**However, the law was adopted in April 2015<sup>36</sup>**, which opened the door to signing the contract. Meanwhile, in March 2015, three years after the first party promotion of the project "Belgrade Waterfront" and 14 months after the official investors' presentation for "the project of national importance," the mayor of Belgrade, in an interview for Tanjug, presented citizens with the first specific information on the form and content of the contract with the future investor for the construction of "Belgrade Waterfront", which in itself speaks about the extent of transparency of this deal: "This land is entered as a share of a legal entity called 'Belgrade Waterfront', where Serbia will continue to be an owner with a minimum of 30 percent, and majority shareholder will, of course, be those who invest the money. The land is not given in ownership to that legal entity, but it is leased for 99 years".

As we have initially predicted, the announcement referred to something that is probably a form of public-private partnerships (joint company of the state and the investor). This joint company would become the lessee of land at 99%, and the facilities would be built according to a plan which would probably also be contracted (then referred period was four years).

**The contract was signed on April 26, 2015.** Instead of clarifying and publishing the contract, Press conference on the signing of the contract for the "Belgrade Waterfront" brought some totally unexpected information. The Mayor said that "the contract will be available to the public",

---

<sup>35</sup> [http://transparentnost.org.rs/images/dokumenti\\_uz\\_vesti/komentari\\_predlog\\_lex\\_specialis\\_bg\\_na\\_vodi\\_mart\\_2015.doc](http://transparentnost.org.rs/images/dokumenti_uz_vesti/komentari_predlog_lex_specialis_bg_na_vodi_mart_2015.doc)

<sup>36</sup> <http://www.transparentnost.org.rs/index.php/sr/aktivnosti-2/pod-lupom/7536-skupstinska-diskusija-o-beogradu-na-vodi>

but only after its approved by the Commission for Protection of Competition. It remained unclear why would the decision of the State Commission in any way have an impact on the public or the confidentiality agreement signed on April 26, 2015, since that Commission cannot change it.

The data published on the signing of the contract for Belgrade Waterfront (the statement with selected data that was distributed to journalists) revealed practically nothing about the job.

Information we could hear or read significantly differ from what we have heard in the last 18 months - instead of 4 years, as announced by the Prime Minister in March, or 10 years, as announced by the Mayor, the construction deadline is 30 years. Construction dynamics is one of the essential elements for the assessment of the overall benefits package for domestic partner. Namely, if the benefit of investments for the state reflects in the possibility of earnings from rental and sale of residential and office space, it is not irrelevant whether the profits of some buildings will begin to be realized in 2020 or in 2040.

In addition, previously talks mentioned investments of about 3.5 billion euros, and on the signing of the contract it was announced that the investor will invest 300 million, of which half through a "loan in the form of a borrowing of the founder," while the rest will be reinvested from profits. In addition, there is reference to an additional agreement on the debt of Serbia for the removal of existing facilities.

What is controversial in the entire business? **Intergovernmental agreements allow the possibility not to implement anti-corruption mechanisms of domestic laws.** But they do not forbid it. And it is not clear why a government that is declaratively committed to the fight against corruption did not want to implement the anti-corruption mechanisms, primarily following the principle of competition and open tender. In the past, the "justification" for the lack of a public tender was that "other people's money must be respected." From what has been presented, it seems that "someone else's money" amounts to 150 million euros, and not to 3.5 billion euros. And we will never know if "someone else's money" could have amounted to more, because there was no competition.

Whose interest is to conclude this job in this way? Concern is that this project is of great political interest for the government and the question is whether we can match the economic interest of the state and political interests of the ruling party. Therefore, there is a reason to worry what will be the control mechanisms in the implementation of the agreement. For example, the previously adopted *lex specialis* allows the investor's exemption from payment of fees for building land but, in return, he will build public facilities. What will be the dynamics of the construction of these facilities in relation to commercial ones and who and how will control the actual cost for building public facilities?

Regarding the imposed dilemma, whether to leave the existing devastated area in Sava amphitheatre, or to build Belgrade Waterfront, it is a false dilemma. It is pointless to ask if anyone supports the existing situation. This is a question of compliance with regulations and the question - if there is an economic benefit from the construction of Belgrade Waterfront, could it have been greater if we had had competition and transparent process. And, of course, the question is what kind of costs would appear in the following decades. The project can undoubtedly bring useful results, if it completes what should have been done in previous years or decades - the completion of Prokop, the ring road and the bridge near Vinca, but the risk is if these projects are financed in a non-transparent way by means of loans that will be part of a "package" with the UAE and the investor. And we could already see that on the signing of the contract - it was announced that the investor will provide a loan of 130 million euros for the state of Serbia for the relocation of facilities from Sava amphitheatre and completion of land expropriation.

Finally, in mid-May 2015 **new "obstacles" for publishing the contract** appeared. In the latest statement of the Mayor, (in addition to opinion of the Commission for Protection of Competition) disclosure was conditioned by some other actions - making a decision on additional capitalization and the contract with the Directorate of land, as well as the approval of the Commission for state aid control.

It is interesting that the Commission for Protection of Competition previously stated that the contract was submitted three days after signing, but that supporting documentation was not delivered and that it was "announced" that the rest will be delivered "as soon as possible." Although the omissions are always possible, it really seems incredible that for such a big project, whose urgent implementation required proposition of a special law under urgent procedure, all necessary documentation was not immediately collected and submitted in order to enable the Commission to decide as soon as possible.

It is also interesting that in a new interview the Mayor makes references how it is necessary for the "Commission for approving state aid" to make a declaration on this agreement (or, in fact, the "Commission for state aid control"). The need for such an approval, or the nature of state aid for which approval is requested (e.g. subsidies, tax exemptions, etc.) have not been mentioned yet.

When analysing what is said on the subject of Belgrade Waterfront, it is evident that the statements **emphasize the transparency and legality of the project**, while it was occasionally **pointed out that large investments are something that is more important than the law**. Noticeably significant was the use of the theme of the project **during the election campaign** - as opposed to the news on the subject throughout the campaign, during the three weeks after the election, **Belgrade Waterfront was almost never mentioned in public**. Finally, when contract details were revealed, significantly less favourable than what was announced in previous years,

some media pointed out the "conspicuous absence" (justified by illness) of the Prime Minister during the signing of the contract that he personally announced for three years. This was followed by the delay of publication of the contract along with new obstacles and preconditions.

It is hard to avoid the impression that in the first phase of the promotion (2012-2014) the main purpose of project presentation was a **political promotion**, and that, for that entire time, **the public received no relevant information**, both on the **legal modalities** of work, and on **its usefulness towards alternative solutions**. This is a step backward compared to the earlier announcement of the project (implementation of regulations that require **transparency and competitive process**, on which the representatives of the ruling party insisted during the campaign of 2012). In the period August 2014 - April 2015 controversial legal steps were taken - from the changes of urban plans, through the adoption of *lex specialis*, to the failure to publish the contract which was justified by suspicious explanations.

How might the case Belgrade Waterfront look like if there was an intention and readiness to fully ensure **competition and transparency**:

- after reaching a (political) decision to implement the idea of "Belgrade Waterfront", an (economic) study on the method of project financing would be made - whether it will be implemented as a public-private partnership with publishing a public competition for the selection of partners, whether it will be self-financed by the state, through a loan and direct debit or potential investors in the public tender will be offered land for construction, etc.

- the manner of realization would be chosen on the basis of the study. Even in the case that at that point there is an investor ready to finance the project, there is no reason not to conduct a public, competitive process and provide opportunity for other potential investors to participate in the race (even if all of them were from the same country with which the interstate agreement was concluded).

- upon selecting the investor, even if the investor is from a country with which there is an interstate agreement on cooperation, there are no legal obstacles to the implementation of anti-corruption mechanisms of the PPP Law, especially with respect to issues such as: timely and public disclosure of (state) cost estimate and the analysis of the obtained value in relation to the invested assets, the assessment of planned risk allocation (whether the state bears the risk if the investor cannot sell 1.8 million square meters of office and residential space), the issue of control over the implementation of the agreement and the commitments.

**Instead**, we had:

- the idea, represented in the election campaign, to implement the project in full compliance with the principles of competition
- post-election (political) decision on the project implementation
- signing the interstate agreement which enabled the project to be implemented without the application of the competition principles
- investor's offer to finance the project which is modified compared to the one initially presented, but of the approximate size and value
- beginning of preliminary work, the news of competitions for the construction of individual buildings within the project, donation for the decoration of the building with the headquarters of the centre for the promotion of the project, up until signing the contract
- the statement that the laws will be obeyed (with no clear reference to any specific laws), but that " the money of investors must respect as well"
- changes in the plan according to the investor's needs
- the adoption of the *lex specialis* for the investor's needs
- signing the contracts and delay of its publication

## **Epilogue**

The contract was finally published in late September 2015<sup>37</sup>. Published documents confirmed its legal nature – it is a type of public private partnership (joint venture). Published provisions are considerably less favourable for Serbian partner than previously announced or expected. For example, even if “value of investment” of 3.5 billion EUR is standard part of every news about the project, it is not mentioned in the contract at all.

On the contrary, there is a value of investment of the foreign partner – 150 million EUR in cash and another 150 million EUR as a loan for the joint venture company. Deadlines to finalize works are also substantially longer than announced – 30 years for the whole project. Publishing of the contract opened also new controversies related to the possibility to buy (not just to rent) city land and in regards to the guarantees for project implementation.

---

<sup>37</sup> <http://www.media.srbija.gov.rs/medsrp/dokumenti/beograd-na-vodi-eb.zip>

Transparency Serbia is non-partisan, non-governmental and non-for profit voluntary organization established with the aim of curbing corruption in Serbia. The Organization promotes transparency and accountability of the public officials as well as curbing corruption defined as abusing of power for the private interest.

Transparency Serbia is national chapter and representative of Transparency International in Republic of Serbia.

Publisher

Transparency Serbia

Palmoticeva 31, Belgrade, Republic of Serbia

Tel: 011 303 38 27

Email: [ts@transparentnost.org.rs](mailto:ts@transparentnost.org.rs)

[www.transparentnost.org.rs](http://www.transparentnost.org.rs)

[www.facebook.com/Transparentnost.Srbija](https://www.facebook.com/Transparentnost.Srbija)

