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Country Procurement Assessment Report

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ACRONYMS & ABBREVIATIONS

ACC	Anti-Corruption Council
CDLS	Center for Liberal-Democratic Studies
CFAA	Country Financial Accountability Assessment
CPAR	Country Procurement Assessment Report
EAR	European Agency for Reconstruction
EBRD	European Bank for Reconstruction and Development
ECA	Europe and Central Asia
ERP	Environmentally Responsible Procurement
ESW	Economic and Sector Work
EU	European Union
FDI	Foreign Direct Investment
FRY	Federal Republic of Yugoslavia
FY	Financial Year
GPA	Agreement on Government Procurement
GRECO	Group of States Against Corruption
ICB	International Competitive Bidding
ICM	Initiating Concept Memorandum
IFI	International Financial Institution
IMF	International Monetary Fund
IS	International Shopping
LPP	Law on Public Procurement
MOF	Ministry of Finance
MOFE	Minister of Finance and Economy
MOJ	Ministry of Justice
MSA	Mutual Services Agency
NCB	National Competitive Bidding
NGO	Non-Governmental Organization
OG	Official Gazette
PEIR	Public Expenditure and Institutional Review
PPC	Public Procurement Commission
RM	Republic of Montenegro
RM MOF	Republic of Montenegro Ministry of Finance
RS	Republic of Serbia
RS MOFE	Republic of Serbia Ministry of Finance and Economy
SAC	Structural Adjustment Credit
SAI	Supreme Audit Institution
SFRY	Socialist Federal Republic of Yugoslavia
SME	Small and Medium Enterprise
TA	Technical Assistance
TI	Transparency International
TSS	Transitional Support Strategy
UN	United Nations
UNCITRAL	United Nations Commission for International Trade Law
USAID	United States Agency for International Development
WTO	World Trade Organization

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OVERVIEW

Introduction

Whilst the Federal Republic of Yugoslavia (FRY) is currently undergoing a period of significant constitutional change, the Republics of Serbia and Montenegro, having recently signed an Agreement to form a new state union of "Serbia and Montenegro," have reiterated their commitment to the unrestricted operation of a "common market" between the two member states and to the free flow of people, goods, services and capital within the new state union. Public procurement will certainly form an important element of that market, as the scale of expenditure on public procurement – about 9 percent of GDP - means that the public sector is a major customer for all sectors of the economy.

The timing of this Country Procurement Assessment Report (CPAR) is particularly appropriate because Yugoslavia, following significant governmental changes, and is now looking outward towards reintegration with regional and global financial and economic systems and the country's new leadership has declared Yugoslavia's aspiration to align itself with the European Union (EU), with the eventual aim of accession. Reform of public procurement legislation will form an essential part of that new direction. Equally important, the new Governments in the Federation and Republic of Serbia have declared their intention to "break with the past," but will win public support in their reform agendas only if they can prudently manage scarce public resources by exerting greater control over procurement expenditures and achieving better value for money in government contracting. The report was discussed at the draft stage and its key findings and recommendations agreed with the Serbian Ministry of Finance and Economy and with the recently-established Public Procurement Commission (PPC) of Montenegro.

This first national assessment of public procurement in Yugoslavia examines all areas of public procurement operations, including the legislative framework, the performance of regulatory functions, the enforcement regime, the capacity of public sector institutions to conduct procurement and the effects of corruption on procurement. The assessment, which was conducted jointly by the World Bank and the European Bank for Reconstruction and Development (EBRD), was carried out in consultation with counterparts from Federal Ministry of Finance, Federal Ministry of Foreign Economic Relations, the Ministry of Finance and Economy of the Republic of Serbia, and the Ministry of Finance of the Republic of Montenegro.

This CPAR forms an integral part of the World Bank's two-phase Transitional Support Strategy (TSS) for Yugoslavia, comprising a first phase that would enable the Bank to provide analytical and advisory assistance, including development of a medium-term recovery program and limited financial assistance under a special Trust Fund for FRY, followed by full assistance intended to follow in the second phase. The CPAR forms part of one of three core pieces of economic and sector work (ESW) being undertaken by the Bank, at the Government's request, and has been undertaken simultaneously with the Country Financial Accountability Assessment (CFAA) and the Public Expenditure and Institutional Review (PEIR). This report attempts to build clear linkages with the findings and recommendations of both those reports.

Overall Assessment

The key findings, including risk assessment, the strengths and weaknesses of the public procurement system currently in place, and the main features of a proposed action plan are summarized below.

Key Findings & Risk Assessment

Procurement has, until recently, been a neglected function.

Up until now, procurement has not been considered to be a core function of government, worthy of specialized staff and dedicated organizational units. However, as Governments, particularly those of the Republic of Serbia and the Republic of Montenegro, have initiated wide-ranging reforms to move to a more market-based economic system and to integrate their economies with those of the European Union, they have begun to attach greater importance to public procurement and have taken steps to enact legal reforms in this area.

Yet public procurement accounts for a significant percentage of public expenditure.

In 2001, the Governments of the Federation and of Serbia together spent some 24 percent of total public expenditure or about 9.5 percent of GDP on public procurement. In Montenegro, public procurement accounted for more than 18 percent of public expenditure or 7.7 percent of GDP during the same period. Therefore, making public procurement more cost effective can save a substantial amount of scarce public resources. Based on experience in other countries, governments can realize savings of as much as 20 percent of total procurement value through competitive public procurement. Price surveys conducted for this assessment suggest than even greater savings may be achieved in Yugoslavia.

The public procurement environment is high-risk.

Based on the analysis of its legislative framework, the effectiveness of its regulatory institutions, the strength of its enforcement regime, the capacity of its institutional and human resources, and the threat of corruption, the assessment found that the environment for conducting public procurement in Yugoslavia is high-risk.

Strengths and Weaknesses

Legal Framework:

There are many gaps and weaknesses in the current legal system in the Federation and Serbia,

The Federation Government has not yet taken any concrete steps to prepare and enact a basic procurement law and current provisions fail to provide an adequate legal basis for the performance of public procurement. Also, in the Republic of Serbia, there are only partial provisions, scattered over various sector-specific enactments, but these do not provide an adequate legal basis for the conduct of public procurement. They fail the key tests of transparency, competitiveness, economy and accountability and provide excessive discretion to public officials in making decisions on awarding contracts.

whereas Montenegro has recently enacted a comprehensive Law on Public Procurement.

Having benefited from a comprehensive program of externally-financed Technical Assistance, Montenegro has already adopted, on 14 August 2001, a new Public Procurement Law. It is built on sound principles and deals with all of the provisions which one would expect to find in a modern procurement law. The Government of Montenegro has expressed its clear opinion that the RM Procurement Law is fully consistent with the Procurement Directives of the European Union (EU).

But Serbia is preparing a new Public Procurement Act.

In Serbia, a new draft Public Procurement Act is currently before the Parliament. This draft law marks a great improvement over the existing legislation. However, while the draft law contains many of the key ingredients for a good public procurement law, there are still a number of critical deficiencies, which should be addressed as part of the consideration of the draft act, in order to make it more comprehensive and to bolster transparency. This report contains detailed recommendations for the improvement of the draft law at Annex G.

Current Practices:

The weakness of the current legislation breeds many abusive practices in public procurement.

The assessment found many instances of bad and abusive practices in public procurement. The planning of public procurement is inherently weak. In many sectors, such as health, there is no effective link between, on the one hand, the supplies of goods which are needed to deliver even basic public services and, on the other, what public institutions buy. Moreover, much public procurement is currently not exposed to competitive bidding, which hinders transparency, facilitates corruption and contributes to poor value for money in expenditures on procurement. Even where public tenders are held, under weak federal and Serbian legislation, they are frequently conducted with opaque procedures, including inadequate periods being allowed to bidders to prepare their bids, which is open to manipulation. The process of bid evaluation is also particularly susceptible to abuse, as evaluation criteria are not disclosed to the bidders - an essential element of transparency - and the work of evaluation committees is undermined by the excessive discretion currently afforded to senior public officials in making contract award decisions.

Organization & Resources:

Authority and responsibility for conducting procurement are not clearly defined.

In the Federation and in Serbia, current legislation generally requires that procurement be conducted by Tender Commissions established in each institution. However, accountability is severely undermined by the fact that these Commissions do not have clear authority to make procurement decisions and by the excessive discretion allowed to senior public officials, who frequently ignore or override the recommendations of the Tender Commissions.

Weak enforcement arrangements allow such abuses to continue.

In the Federation and Serbia, responsibility for enforcement of current procurement legislation is not clearly vested in any specific institution and, as a result, enforcement is weak and compliance low. While the new draft Public Procurement Act of Serbia foresees the establishment of a specialized, independent Public Procurement Office, it will not be operational for at least a year. No regulatory functions are being conducted at the level of the Federation.

Montenegro has set up a new regulatory body for public procurement

In Montenegro, a new regulatory body, the Public Procurement Commission (PPC) has recently been established and has started work. However, it is as yet under-resourced and is in need in strengthening.

Capacity to conduct procurement is weak.

At all levels of administration, untrained, non-specialist staff handle procurement, often improperly, which compounds the weaknesses in the legislation. Montenegro has at least begun to train public officials in procurement, though many people, especially at the local government level, still need training. At the Federation level and in Serbia, most public officials who handle procurement have received no training at all for the task.

The rights of bidders are inadequately protected

Because, in the Federation and in Serbia, there is no formal mechanism in place for the administrative review of bidders' complaints, public officials who violate the current legislation are not being held accountable and bidders' rights are not being protected. The new Montenegrin Procurement Law contains an administrative review procedure, but the mechanism is still not working satisfactorily.

and both internal and external controls over procurement are very weak.

The absence of internal audit functions at all levels of administration is a major gap in the current framework for accountability. Also, the absence of Supreme Audit Institutions (SAI) at both federal and republic levels means that procurement decisions are not being subjected to independent scrutiny.

<u>Anti-Corruption</u>

Procurement-related corruption is a major problem.

Recent survey evidence indicates that corruption "permeates every aspect of societal life in Serbia" and that corruption in public procurement is "exceptionally intensive." The health sector is regarded as the "epicenter"[1] of procurement-related corruption. To their credit, the Governments of Serbia and Montenegro have recently demonstrated commendable vigor in tackling corruption: both republics participate in the Stability Pact Anti-Corruption Initiative (SPAI) and both have initiated meaningful steps to combat corruption. The preparation of the new draft procurement law in Serbia is one of a package of five laws aimed at tackling corruption.

[1] "Corruption in Serbia" Center for Liberal-Democratic Studies, page 41.

Private Sector:

The private sector has little faith in the fairness of public tenders.

Most bidders, especially small and medium enterprises (SMEs), do not pursue public-sector contract opportunities because they have a low level of confidence in the conduct of public tenders. They worry about the wasted time and cost of bidding, as well as about arbitrary or corrupt contract award decisions.

Summary of Recommendations and Action Plan

Legislative Reform:

Clear procurement rules should be included in the Acts governing the new State Union institutions.

Because no move has yet been made to enact a public procurement law at the Federation level and given the anticipated constitutional change from the Federal Republic to a state union, it is recommended that the founding acts which establish each of the new state union institutions should contain clearly defined procurement regulations. These regulations should be harmonized as fully as possible with the Serbian and Montenegrin procurement laws.

A state union law on public procurement should be a medium-term aim

Over the medium term, a specific law on public procurement should be enacted at the state union level. The procurement laws of the two republics should be reasonably harmonized with it, in order to achieve a common public market and to facilitate alignment with the EU.

Procurement of non-military items by the defense forces should come under the civil procurement legislation

Because the bulk of expenditure at the Federation – and future state union – level is on defense and because a sizeable proportion of that expenditure is on non-military goods, works and services, it is recommended that such non-military procurement should be government by the civil procurement legislation, as it is in other countries.

Serbia should give priority to enacting an improved Public Procurement Law.

The new draft Public Procurement Act of Serbia should be enacted as soon as possible, with the amendments proposed in this report, which were discussed and agreed with the Serbian Ministry of Finance and Economy in June 2002, included to make it more comprehensive and to provide a firmer base for transparency, accountability and competitiveness.

Procurement laws in Serbia and Montenegro should be supported by comprehensive implementing regulations

A comprehensive set of implementing regulations are required to underpin the new Public Procurement Law of Montenegro and these should be adopted as a matter of priority. In Serbia, once the new draft law has been enacted, implementing regulations will also be required there.

and standard procurement documents.

In both Serbia and Montenegro, a comprehensive set of standard procurement documents for goods, civil works and services should be developed and their use by all public procuring entities made mandatory. Such standard documents should significantly improve the ability of public officials to conduct procurement accurately and effectively.

Organizational Reform:

Responsibility for conducting procurement should rest with individual institutions

At the level of the new state union institutions, responsibility for conducting procurement should be decentralized to each institution. However, each institution should have the freedom to appoint another institution to conduct procurement on its behalf. A successor organization to the current Federal Mutual Services Agency (MSA), which could be appointed to conduct procurement on behalf of state union institutions, may offer a cost-effective option. Decentralized authority to each individual public institution should continue in Serbia and Montenegro.

New and stronger regulatory institutions are needed to improve enforcement.

The Mutual Services Agency (MSA), which will perform regulatory functions under the new Serbian procurement law until the establishment, after a year, of the new Public Procurement Office (PPO), should be strengthened to increase its capacity to perform these essential functions in the short term. The Serbian Government should establish the new PPO as a matter of priority and it should benefit from the Technical Assistance currently being planned by the European Agency for Reconstruction (EAR). In Montenegro, the new Public Procurement Commission (PPC) should be strengthened by increasing its staffing and facilities to enable it to perform its functions effectively.

Training and Capacity Building:

Training initiatives should take place within a planned environment

It is recommended that, given the large number of officials requiring training, a comprehensive training strategy should be developed in Serbia, Training should be based on an approved curriculum for public procurement, with graduated levels of complexity.

and institutions identified to provide procurement training over the long term

Serbia should identify institutions, such as universities, which can launch public procurement training courses and completion of such courses should be required of public officials who handle procurement as a major part of their jobs. Twinning relationships should be established between local training institutions and internationally recognized procurement training institutes, to facilitate the develop of curricula and training materials. A professional institution should be established to develop procurement as a profession in its own right.

Control Environment:

Internal and external audit control over procurement needs to be strengthened at all levels

At state union, Serbian and Montenegrin levels, internal audit functions should be established in major spending institutions, to check on the compliance with procurement procedures with the legislation. Given the absence of SAIs, Governments should employ qualified independent auditors to carry out annual audits of procurement.

and administrative review of bidders' complaint should be provided

To improve planned measures to hold public officials accountable for procurement decisions, in Serbia the function of performing administrative review of bidders' complaints should be added to the authorized functions of the new Public Procurement Office (PPO) in the current draft Procurement Act.

A system of training public officials in procurement should be established.

Both Serbia and Montenegro should develop training strategies for public procurement, covering all levels of administration and with the objective of creating a training system which is sustainable over the long term. Educational institutions, such as universities and technical colleges, in key centers should be identified which will set up and deliver an agreed curriculum for public procurement training. In Montenegro, current training programs should be extended to serve public officials at the local government level. The procurement training capacity already built up in the Faculty of Law should be expanded by forging links with Western, particularly European, training institutions, in order to develop curricula and course content for procurement. Once Serbian training institutions for public procurement have been identified, these should also benefit from such twinning relationships. Serbia should make its procurement training institutions available to officials from the state union institutions.

A. PREFACE

A.1 Date, Basis and Scope of the Report

This report was completed on June 24, 2002.

This report is based on the results of interviews with more than 40 public institutions and private companies during three missions to Yugoslavia during July - November, 2001. The missions held discussions with public sector institutions at the federal level, in the Republic of Serbia and in the Republic of Montenegro, as well as with local authorities in both republics, and interested Non-Governmental Organizations (NGOs). This procurement assessment also analyzed a comprehensive range of laws, documents, completed questionnaires, reports and other information collected by the missions.

The assessment encompasses the Federal Republic of Yugoslavia (FRY), the Republic of Serbia and the Republic of Montenegro, but excludes Kosovo, a province of Serbia which is currently under United Nations (UN) administration.

This report was prepared jointly with the Country Financial Accountability Assessment (CFAA) report on FRY and attempts to build clear linkages between the findings and recommendations of that report and public procurement. In addition, this report was written simultaneously with the Public Expenditure and Institutional Review (PEIR) of FRY, and draws on that report where appropriate, particularly in the section on Public Sector Management Performance.

This report was prepared in accordance with the World Bank's internal instruction on the preparation of Country Procurement Assessment Reports (CPARs). The Initiating Concept Memorandum (ICM) for this CPAR identified the following priority issues:

- assess the current legislation governing public procurement at the three levels: Federation, Republic of Serbia and Republic of Montenegro, including the degree of compatibility between them. Such an assessment is essential not just to inform the international community, including the World Bank and EBRD, of the current legislative position, but also because the scoping mission revealed a low level of awareness among Government officials of the legislation which governs their actions in procurement expenditures;
- assess the commercial laws and laws on concessions;
- identify the need for future legislative reform in the area of public procurement;
- examine the foreign trade aspect of public procurement, particularly to define what further reforms will be necessary to enable Yugoslavia to meet its stated objectives of joining the WTO and the EU and to provide the Government with a clear roadmap toward these objectives;
- quantify the current level of expenditure on public procurement, and identify the main opportunities for savings, not only to improve cost effectiveness but also to help the new Government earn a reputation for integrity and good governance. While it was agreed that a national assessment of this sort was beyond the scope of the CPAR, an assessment of at least one key sector should be attempted;
- set standards for public procurement applicable to both federal and republic levels, while recognizing that some parties might have farther to travel to attain those standards than others;

- examine implementation arrangements and institutional strengthening requirements for projects financed by the World Bank and EBRD.

A.2 Acknowledgements

The mission members wish to acknowledge the extensive cooperation and assistance received from officials and staff of the public organizations, state agencies, NGOs and private companies interviewed. Mr. Christiaan Poortman, Country Director, Mr. Tim Gilbo, Country Officer and Ms. Mary Sheehan, formerly Lead Country Officer, offered invaluable guidance on the scope and overall direction of the assessment. Mr. Ardo Hansson, Senior Country Economist, and Mr. Bill Dorotinsky, Senior Public Sector Specialist, offered invaluable comments on the draft report. Mr. Sergei Shatalov, Senior Economist, Mr. Juan Carlos Ginarte, Research Analyst, and Mr. Bazarvaani Darinchuluun, Consultant, assisted with data collection and analysis for the quantification of public procurement expenditures. Mr. Siew Chai Ting, Senior Financial Management Specialist and Mr. Roberto Tarallo, Senior Financial Management Specialist, who conducted the related Country Financial Accountability Assessment (CFAA), provided essential inputs to the assessment and the report on accountability and auditing issues. Ms. Laura Rose, Senior Economist (Health) and Mr. Andrej Huljev, Consultant, assisted with the survey on health sector procurement. Mr. Robert Hunja, Senior Procurement Specialist, Procurement Policy and Services Group, acted as peer reviewer for the report. Mr. Rory O'Sullivan, the Bank's Country Manager in Yugoslavia, Ms. Elaine Patterson, formerly Acting Resident Representative in Yugoslavia, and the staff of the Bank's Belgrade office offered the mission invaluable assistance, especially Ms. Zana Ivanovic, who helped in arranging the mission's program. Ms. Ana Cristina Hirata and Mr. Mohammad Ilyas Butt assisted with the formatting of the report.

A.3 Participating Government Organizations

The main counterpart organizations participating in the assessment were the Federal Ministry of Finance, Federal Ministry of Foreign Economic Relations, the Ministry of Finance and Economy of the Republic of Serbia, and the Ministry of Finance of the Republic of Montenegro.

The preliminary findings and recommendations of the report were discussed during the missions with Professor Dr. Jovan Rankovic, Federal Minister of Finance, Dr. Dejan Popovic, Deputy Minister of Finance and Economy of the Republic of Serbia, and Dr. Milan Dabovic, Assistant Minister of Finance of the Republic of Montenegro. At the time of the later mission, in November 2001, the Serbian Ministry of Finance and Economy was engaged in drafting a new Public Procurement Act but had not previously been performing regulatory functions over public procurement. In Montenegro, while a new Public Procurement Law came into effect in August 2001, the Public Procurement Commission (PPC), which that law establishes as the regulatory body for public procurement, had not yet been established. Therefore, the assessment team's discussions in Montenegro were undertaken with the Ministry of Finance, which bore responsibility for public procurement until the establishment of the PPC. However, because neither Ministry had been actively exercising regulatory functions over public procurement, the concerned officials were not fully engaged in public procurement at the time of the mission's visit and this limited their degree of participation to some extent.

Following submission of draft report to the Governments in May 2002, the draft was discussed with Dr. Dejan Popovic, Deputy Minister of Finance and Economy of the Republic of Serbia, and

with Mr. Niko Nikcevic, President of the Public Procurement Commission of the Republic of Montenegro, in a series of meetings held in Belgrade and Podgorica in June, 2002.

A.4 World Bank – EBRD Team

The joint team from the World Bank and the European Bank for Reconstruction and Development (EBRD) which worked on this report comprised Mr. Shaun Moss, Senior Procurement Specialist, Europe & Central Asia Region, the World Bank, Task Team Leader; Mr. Ian Nightingale, Deputy Director of Procurement and Technical Services, EBRD; Mr. Simeon Sahaydachny, Procurement Legal Consultant; Mr. Milan Parivodic, Legal Consultant (Federal Republic and Republic of Serbia); and Dr. Milorad Ivovic, Legal Consultant (Republic of Montenegro).

B. BACKGROUND

B.1 Country Context

B.1.1 A Democracy in Transition

Until early 1990s, the former Socialist Federal Republic of Yugoslavia (SFRY) consisted of the federation of Bosnia, Croatia, Macedonia, Montenegro, Serbia and Slovenia. In the early 1990s, following the breakup of the SFRY, five republics were established: Slovenia, Croatia, Bosnia-Herzegovina, the Former Yugoslav Republic (FYR) of Macedonia, and the Federal Republic of Yugoslavia (FRY). The SFRY ceased to be a member of the World Bank Group in February 1993.

The FRY was constituted in April 1992 as a federation of the Republics of Serbia and Montenegro and consists of three levels of government: federal, Serbian, and Montenegrin. The Republic of Serbia is by far the larger of the two constituent republics, with 94 percent of FRY's population of 10.5 million and a similar share of its GDP. The Republic of Serbia includes the two autonomous provinces of Kosovo and Vojvodina, (see IBRD Map No. 31506). After the war in Kosovo, this province was placed under the UN administration by UN Security Council Resolution 1244 (June 1999), which established a transitional authority: the United Nations Mission to Kosovo (UNMIK). For administrative purposes, the Republic of Serbia is divided into 29 districts, although some of these lie within Kosovo.

The decade since its founding has been one of regional conflict and international isolation, characterized by authoritarianism and substantial mismanagement of public resources. Federal elections in October 2000, and Serbian Parliamentary elections in December 2000, brought to office reform-oriented governments with a mandate to bring about greater democracy, modernization and integration with the international economy.

The initial CPAR mission took place about a year after the 2000 elections. The CPAR team found the country in transition, not only to a market and a post-conflict economy, but also to a peculiar and uncertain conception of statehood. Considerable progress has been made in establishing democratic governance and in reintegrating the country into the international community. The FRY has been admitted to the United Nations (UN), the Organization for Security and Cooperation (OSCE), the European Bank for Reconstruction and Development (EBRD), the International Monetary Fund (IMF), and the World Bank (WB). On July 23, 2001, a European Union (EU) FRY Consultative Task Force was inaugurated as the first step towards reaching a Stabilization and Association Agreement with the EU. The FRY is a member of the EU's Stabilization and Association Process which aims to create, over time, democracy, peace, stability and prosperity in the Balkans. The FRY also aspires to be a candidate for membership in the EU.

Both the federal government and the republican governments of Serbia and Montenegro have made substantial progress with their economic reform agendas over the past year. In Serbia, progress since elections in December 2000 has been extensive, with wide-ranging liberalization of prices, foreign trade and foreign exchange; tax reform; improved privatization and bank restructuring regimes; enhanced transparency in the budget process; and reductions in the gray economy and smuggling. Although in Montenegro reforms began earlier, supported by technical and financial assistance from external donors, implementation in some areas has been less rapid,

in part because of more serious capacity constraints. All three governments face the daunting task of rebuilding an economy while implementing a tough reform agenda. The renewed commitment to reform in the FRY is substantial, but counterbalanced by uncertainty and risks.

B.1.2 Constitutional Crisis

Foremost among these risks is the future of the FRY and the governance structure of the Republic of Montenegro, both of which remain in doubt. FRY's federal structure is highly decentralized and fluid. The federal Constitution grants the republics many powers not vested in the Federation, including most revenue-raising and most economic and social functions. It reserves as the main federal responsibilities foreign relations, including foreign trade, defense, monetary/exchange rate policy, and customs. In some areas, the reality differs from its legal form; at present, in fact, the federal government exercises these powers fully only over the territory of Serbia (excluding Kosovo, which has been under UN administration since June 1999).

The Government of Montenegro has taken over most of the responsibilities for economic management in its territory, foreign relations, currency and customs, and has largely cut fiscal links with the federal government and the government of the Republic of Serbia.[2] Well before the federal elections in October 2000 and Serbian elections in December 2000 that brought to office the first federal and Serbian reform-oriented governments, Montenegro had already elected a reformist government that was moving to separate itself from the rest of the FRY, with the strong support of the international community. In 1998, federal authorities ceased transfers of sales and excise taxes due to Montenegro, prompting Montenegro to take control of its revenue sources. In 1999, Montenegrin officials were excluded from the work of the NBY, prompting Montenegro to introduce the German Mark (DM) as a parallel currency with the Dinar in November 1999. The DM became the only legal tender a year later and was then succeeded by the Euro in January 2002. Montenegro also took control of its borders and customs administration and set up a council to establish monetary and foreign currency policy; Belgrade countered by temporarily imposing a trade blockage against Montenegro and terminating electronic payments between the two republics through the centralized payments system. Montenegro established its own central bank, the Central Bank of Montenegro (CBM) in November 2000. The trade blockade has been lifted and NBY has since moved to reestablish a payment system between Serbia and Montenegro.

The federal and Serbian governments established mechanisms for joint preparation of new legislation and policy discussions, and in August 2001, the federal government adopted "The Initial Grounds for the Joint Platform on Constitutional Restructuring of the FRY." A political dialogue was ongoing between Montenegro and Serbia to determine the nature of their constitutional relationship. Long-awaited talks between the federal institutions and the Republic of Montenegro broke off in late October 2001 without agreement on how to run jointly a federal Yugoslav state. With EU mediation, Serbia and Montenegro signed an agreement in Belgrade on March 14, 2002, "The Basis for the Settlement of Relations between Serbia and Montenegro," which will lead to the replacement of the FRY with an even looser state union, to be called Serbia and Montenegro.

[2] This paragraph is based on section 3 of ESI Report: "Sovereignty, Europe and the Future of Serbia and Montenegro, A Proposal for International Mediation" February 12, 2001.

The future of the FRY has been uncertain for some time, and a great deal of political energy has been devoted to constitutional issues. It is hoped that the administrative streamlining and clarification of responsibilities under the new agreement will free resources to flow into critical economic and public sector reform efforts.

B.1.3 Governing Structures

Apart from the constitutional issues, there are two major obstacles to the proper functioning of existing governing structures: (i) significant duplication of functions in the federal and Serbian governments, amounting to about 20 percent of the 2001 federal budget,[3] and (ii) lack of harmony between the federal and Serbian Constitutions. The Serbian constitution was adopted on September 28, 1990, at a time of state and political crises in the former SFRY, and that Constitution was not subsequently made concordant with the 1992 Constitution governing federal institutions.

The federal government is based on the separation of powers between the executive— prime minister, deputy prime minister, and federal ministers—the legislative body, the federal Parliament, and the judicial branches, including the federal Supreme Court and federal Public Prosecutor. The Parliament is bicameral and consists of a Chamber of Citizens (deputies elected in the member republics in direct elections, by secret ballot, provided that in the member republics no fewer than 30 federal deputies can be elected), and a Chamber of the Republics (consisting of 20 federal deputies from each member republic). The Parliament decides, among other things, about joining international institutions and passes the federal budget, approves the federal balance sheet, ratifies international treaties within the competence of the FRY, and elects and dismisses federal-level executives, including the governor of the NBY. The NBY is an independent entity and the sole issuing institution of the monetary system of the FRY, responsible for monetary policy, exchange rate stability, and for financial discipline and performance of other operations prescribed by federal laws.

Both the Republic of Serbia (capital in Belgrade) and the Republic of Montenegro (capital in Podgorica) are unitary republics headed by a prime minister, with a single assembly (National Assembly) and a directly elected president. Each republican government consists of a prime minister, deputy prime ministers, and ministries. The National Assemblies are the representative and legislative bodies of the republics. The National Assemblies pass all laws of the land, ratify international treaties falling within the competencies of the republics, appoint the Prime Minister, ministers, and justices of all courts, adopt the budget, and perform other duties as established by the Constitution. The differences between the two republics are that (1) Montenegro's Constitution (October 12, 1992) provides for decisions related to changes in constitutional status or to an alteration of borders to be subject to citizen referendum, and (2) since its move to de facto independence, Montenegro conducts its own foreign policy, concludes international treaties, and carries out other powers that in Serbia’s case are exercised by the federal government.

[3] Based on a Survey of Replication of Functions in Federal and Republic Bodies and Levels of Funds for Financing, jointly prepared by the Federal MOF and Serbian MOFE.

B.1.4 Economic Governance

Economic transition in the FRY is taking place under extremely difficult conditions. Output, which has only partly recovered from the economic devastation caused by the Kosovo war, stands at about half of its 1990 level. The country's infrastructure is in disrepair following years of inadequate investment and the damage inflicted by NATO bombing. Unemployment, when measured in a consistent and internationally comparable way, is not nearly as high as is reported by official statistics (around 30 percent in 2000), although it is on a rising trend.[4] The impact of armed conflicts has been particularly severe, with an estimated 630,000 refugees from Bosnia-Herzegovina and Croatia, and internally displaced persons from the province of Kosovo (totaling around 6 percent of FRY's population.[5] Serious energy shortages are being somewhat alleviated with humanitarian assistance. Much-needed structural reforms were stalled until 2001.

B.1.5 The Yugoslav Legacy

The Yugoslav economic system was far more market-oriented than those of other Eastern European state-run economies. Unlike the system prevailing in the Warsaw Pact countries, in fact, the Yugoslav system did not rely on central planning and its enterprises were run by both managers and their employees, who were free to make their own price, external trade and investment decisions. Banks were not an instrument for central planning but were owned by enterprises and managed in a decentralized manner. Thus, the SFRY was spared the worst features of central planning, particularly administrative price-setting and state control over trade flows.

The so-called self-management or social-ownership system, with its two-tier banking system (Central Bank and commercial banks) and free pricing mechanism for most consumer goods, allowed degrees of competition beyond those existing in the Warsaw Pact countries and generally avoided the shortages of consumer goods characteristic of those economies. Consequently, in comparison with other state-run economies, the SFRY presented a relatively developed private sector and a higher share of services in its overall economic structure. However, the model underlying the structure of social ownership presented unclear governance arrangements: ownership rights belonged to "the society" (i.e. no clearly identified owners), while day-to-day management was in practice entrusted to boards of Associated Labor (a combination of employees and managers). Also, a number of distortionary policies shielded selected inefficient sectors/enterprises from competition (e.g. poorly performing industrial sector enterprises), leading to higher costs for domestic producers, which were, in turn, partially offset by a system of direct subsidies.

B.1.6 War and Economic Sanctions

The Balkan power struggles, armed conflict, and international sanctions shattered the already fragile economy of the FRY. UN-imposed economic sanctions (embargoes on trade, travel, and transportation) on Yugoslavia for its involvement in the wars in Bosnia-Herzegovina and Croatia

[4] World Bank: "Breaking with the Past: The Path to Stability and Growth – Volume I; The Economic, Social and Institutional Reform Agenda" Box 1.2

[5] Idem, paragraph 1.15.

were in effect from 1992 until 1996. The U.S. and other countries maintained an "outer wall" of sanctions affecting membership in some international institutions, demanding that the Yugoslav cooperate with the war crimes tribunal in The Hague (2001), and addressing concerns about human rights in Kosovo and other important issues. Owing to the escalation of ethnic tensions in Kosovo, in mid-1998 the U.S. and the EU imposed bans on new foreign investment in Yugoslavia and on financial transactions by Yugoslav entities, while the EU revoked the trade preferences that it had earlier granted. The confrontation over Kosovo culminated in a North Atlantic Treaty Organization (NATO) bombing campaign from March to June 1999, at which time the EU and the U.S. also imposed a ban on oil sales. The EU sanctions were also observed by 14 other European countries. The sanctions eventually started being lifted in October 2000, following important political changes in the FRY.[6]

Yugoslavia's economic standing has fallen from one of Eastern Europe's most prosperous countries in the 1980s to one of its poorest today, reflecting the effects of wars and years of economic isolation. Serbia once had the strongest economy in Yugoslavia, with the greatest potential to grow based on market size and resources. Today, Yugoslavia's per capita GDP is well behind that of other former constituent republics of the SFRY, which have fared much better since achieving their independence (e.g. Slovenia, Croatia) and ranks Yugoslavia as being among Europe's poorest countries.

The devastating effect of the NATO bombings and the Kosovo crisis on the country's economic performance is further reflected in the figures for social product. Social product recorded modest growth in the mid-1990s, stalled in 1998 and collapsed by 21.9 percent in 1999 (see Table 1). Social Product, a traditional Yugoslav economic measure, differs from GDP in that it omits government services.

Table 1: Yugoslavia's Social Product, 1995-1999[7]

	1995	**1996**	**1997**	**1998**	**1999[(a)]**
Total Social Product at constant 1994 prices (YuD m)	22,017	23,310	25,028	25,652	20,045
Real change (%)	6.1	5.9	7.4	2.5	-21.9
Social Product per capita (YuD) at constant 1994 prices	2,088	2,200	2,361	2,416	1,886

[(a)] excludes Kosovo.

B.1.7 A New State Union: Serbia and Montenegro

The FRY was constituted in April 1992 as a federation of the Republics of Serbia and Montenegro and consists of three governments: federal, Serbian, and Montenegrin. A historic agreement was signed in Belgrade on March 14, 2002, "The Basis for the Settlement of Relations between Serbia and Montenegro," based on which Yugoslavia would be replaced with an even looser "state union" to be called simply Serbia and Montenegro. The FRY would cease to exist.

[6] ICG Balkan Briefing – Sanctions Against The Federal Republic of Yugoslavia (as of October 10, 2000).

[7] Economist Intelligence Unit

The next step is ratification of this agreement by the three existing Parliaments, adoption of referendum laws by the two member states and promulgation of a Constitutional Charter.

Under the agreement, the new union would have some smaller common institutions, including a presidency, a Parliament and a Council of Ministers, but each side would keep its own political and economic systems. Upon the promulgation of the Constitutional Charter, laws on the election of parliamentary representatives would be adopted by the two member states, in compliance with principles defined by the Charter. Elections would then take place and a Parliament of Serbia and Montenegro constituted, which would then elect the president. The president would propose the composition of the Council of Ministers and direct its work. The Council of Ministers would have five departments: foreign affairs, defense, international economic relations, internal economic relations and protection of human and minority rights. The member states would jointly finance these common functions. The agreement envisages that the Army of Serbia and Montenegro would be under the command of a Supreme Defense Council, composed of three presidents and making decisions by consensus.

The March 2002 agreement thus recognizes the current state of affairs on both the economic and political planes: that there is one country and two independent economies, currencies (the Euro and the Yugoslav Dinar), separate banking systems, separate customs tariffs and customs services, separate fiscal rates and fiscal services. Under the agreement, each economy would be responsible for its own debts, and for its policies vis-à-vis international financial institutions. The two member states also have the right to reconsider the agreement after three years and may then institute proceedings for a change in the status of the state, that is, withdrawal from the state union.

An important outcome of the agreement is the reduction in administrative costs, because the oversized federal apparatus, which was being financed by Serbia alone, would be done away with. Most federal and Serbian republican institutes and directorates would merge, which is expected to result in the creation of a single, efficient Serbian administration.

As this report is being finalized, the agreement has been ratified by the Republican and federal parliaments, and a constitutional commission has been appointed. The Constitutional Charter has not yet been promulgated, the shape of the new common institutions is not finalized, and the merger of the federal and Serbian institutions has not commenced. This report was prepared starting five months prior to the March 2002 agreement. Even after the constitutional rearrangements set out in the agreement, the findings and recommendations will continue to be valid. In order not to delay the impact of its recommendations on the reform agenda, the report's original structure and nomenclature (federal institutions and two republics) have been retained. Because of the fluidity of the situation, the Bank wishes to remain in continuous dialogue with all three governments as the new arrangements take shape and to update its recommendations in light of changing circumstances.

While the process of moving to the new institutional and governance arrangements is not expected to give rise to additional fiduciary risks or that the new institutions would be less robust than the current ones and would require additional special safeguards, the Bank nevertheless wishes to ensure that the transition is as well managed as possible from a fiduciary perspective. It is, therefore, proposed to update this assessment within an appropriate period of time, probably no later than two years from the date of this report.

B.2 World Bank Portfolio in Yugoslavia

Following the Government's request, the Bank embarked on a two-phase Transitional Support Strategy (TSS) for Yugoslavia. The first phase would enable the Bank to provide analytical and advisory assistance, including development of a medium-term recovery program and limited financial assistance under a special Trust Fund for FRY (established by the Bank's Board of Directors on March 13, 2001). In the second phase, once membership in the World Bank was established, FRY would benefit from temporary exceptional access to up to US$540 million of IDA funds over three years, with actual lending to be determined on policy performance. In FY02 analytical and advisory assistance includes three core pieces of economic and sector work (ESW): firstly, a three-part assessment of public expenditure, financial accountability, and public procurement; secondly, a private-sector development strategy; and, thirdly, a poverty-focused household survey.

At then end of June 2002 the World Bank's portfolio comprised 5 grants with a total value of US$30 million, and four IDA credits with a total value of US$171.5 million (see Annex A).

B.3 EBRD Portfolio in Yugoslavia

The EBRD has recently approved several projects, including major infrastructure loans for the transport and power sectors, investments in local banks in support of Small and Medium Enterprises (SMEs) and working capital for private companies. A detailed list of the EBRD's loan portfolio in Yugoslavia can be found in Annex B.

The EBRD expects to increase its private sector operations, particularly long-term loans and equity investments as the privatization process gains momentum in Serbia and Montenegro. New investment is aimed at helping create clearer ownership and corporate governance of companies. The EBRD is also assisting the Government of Serbia to achieve further legal and regulatory reform, especially in the area of secured transactions.

C. FINDINGS

PUBLIC SECTOR

This section reviews the main legal enactments which govern public procurement and records the scope of applicable instruments and the extent to which legislation is accessible to the public.

C.1 Legal and Regulatory Framework

C.1.1 The Legislative Inheritance of the Federal Republic of Yugoslavia

Yugoslav law is based on code rather than on case law and belongs to the Germanic family of the continental legal system. In civil law, major influences can be traced from the General Civil Code of Austria, the German civil law, and the Swiss Code of Obligations by way of three landmark civil codifications on the respective territories of the Kingdom of Yugoslavia up until 1946: Austria (1811), the Civil Codes of Serbia (1844), and Montenegro (1888). In the field of business law, influences of international legal instruments (conventions, model laws, uniform terms) and common law (English and US commercial law) are gaining momentum.

With the establishment of the Socialist Federal Republic of Yugoslavia (SFRY), the entire legal system of the pre-war Kingdom of Yugoslavia, including the three civil codifications, was repealed. Features of the SFRY legal system which still cause complications for commercial and business operations include: confiscation and nationalization of private assets; imposition of ownership maximums for agricultural land and residential property, which resulted in widespread divestiture; State ownership of companies, which provided their assets, workers' self-management, and the linked, constitutionally-based notions of "social property.", which became the main entities engaged in economic activity, instead of privately-owned companies. All of these factors fostered a lack of accountability for the financial well-being of corporate entities. However, the legal system of Yugoslavia has been in transition since the political changes of October 2000. Inherited problems and inefficiencies persist in most areas of law: constitutional, administrative, commercial, civil, and criminal. Still, the state administration has been particularly slow to reform, which has hindered the development of public procurement in Yugoslavia.

C.1.2 General Aspects of the Development of the Legal Framework

The current of development of the legal framework for public procurement reflects the separate approaches which the two republics of Serbia and Montenegro have taken to legal reform in recent years. The Republic of Montenegro has drafted, with assistance from the United States Agency for International Development (USAID), and enacted in August 2001, a Public Procurement Law (RM Official Gazette No. 40/2001), which supercedes the fragmented legislation which Montenegro had inherited from the SFRY.

In the Republic of Serbia, partial provisions, scattered over various, mostly sector-specific enactments, still apply to procurement but the Parliament is quite advanced in the process of adopting a new Public Procurement Law. Meanwhile, the Federal Republic has yet to take concrete steps to prepare and enact a basic procurement law. Given the imminent constitutional

changes, described above, it is probable that the Federation will not act soon to prepare such a law. However, it does seem likely that the state union will require its own enactment on public procurement to govern procurement expenditures made by the new institutions to be established at that level.

In the absence of a comprehensive legislative framework in the Federation and Serbia, issuances of normative and regulatory texts on public procurement have been sporadic and cover only partially the range of issues which should be dealt with in a comprehensive legal framework for public procurement.

C.1.3 Legal Instruments Issued to Date

Federation: The only procurement-specific texts at the Federal level were issued more than twenty years ago, in the former SFRY. These texts contain only general provisions and do not set forth in an adequate manner the kinds of public procurement rules and procedures required by a Government seeking to operate in a market economy. These include:

- Regulations on terms and conditions for procurement, usage, maintenance, keeping, and protection of objects of artistic and cultural value which are in use by Federal bodies;[8]

- Regulations on terms under which transportation vehicles not manufactured in SFRY may be obtained for the needs of Federal bodies.[9]

- Some provisions pertinent to public procurement are found in the Law on Property of FRY which provides that assets should be procured, sold or leased by public tender based on the collection of offers and, exceptionally, by direct negotiation. The Federal Government regulates the types of assets which may be procured or sold by direct negotiation.[10]

Republic of Serbia: General references related to public procurement are found in the Law on Budget Execution and the Law on Public Revenues and Public Expenditures, as well as in the Decree on the Administration of Mutual Services, which contains broad provisions on how the Mutual Services Agency (MSA) should conduct procurement operations on behalf of various organs of the Serbian Government. However, these provisions primarily determine who is authorized to make decisions about procurement; they do not set down a clear set of rules as to how procurement is to be conducted. In addition, the following enactments contain more specific procurement-specific provisions:

- the Regulation on Types of Movables which may be Procured and Sold by Direct Negotiation and Defining Equipment of Larger Value, adopted in 1996 pursuant to the Law on Assets in Ownership of Republic of Serbia, provide that all levels of government may apply the direct negotiation procurement method for (1) equipment and inventory, the unit value of which does not exceed 50,000 YuD (US$775) (2) stationary and small inventory, tools and spare parts, the procurement of which is necessary to prevent interruption of work; (3) books and literature for library needs and (4) other movables necessary for the operation of government bodies.

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[8] OG of SFRY no. 62/81; amended, OG of SFRY no. 11/97.
[9] Official Gazette of SFRY, no.25/81.
[10] Official Gazette of FRY no. 41/93.

- the RS Law on Construction of Objects provides that the development of technical documentation and construction of buildings may be awarded by one of three procurement methods: public tender, collection of offers or direct negotiation. The law affords the procuring entity discretion to decide which method to apply to each procurement transaction. If the procuring entity opts for either the public tender or collection of offers method, then the Regulations on Terms, Manner and Procedure for Granting Approval for Construction of Objects, issued by the Minister of Construction in 1997 (Official Gazette RS 25/97) apply [hereinafter called RS Building Construction Regulations]. These Regulations deal, in a general and very brief manner, with two types of procurement methods: public tendering and a variant of that method preceded by an open call to apply for prequalification. The Regulations contain provisions on:

  a) invitations to bid;

  b) information required to be provided to bidders, though no mention is made of doing so by way of bidding documents;

  c) required submission by bidders of extracts from their company registry;

  d) a cross-reference to the Law on Building Construction which limits participation in bidding on construction contracts to companies satisfying the requirements of that Law;

  e) a requirement that a minimum of three bids must be received for the tender to be concluded;

  f) the role of the tender committee to provide the procuring entity with a recommendation for award;

  g) decision-making by the procuring entity; and

  h) some provisions on record keeping and mandatory reporting.

- A substantively similar instrument, Regulations on Terms, Mode and Procedure for Granting Approval for Development of Technical Documentation, for Works on Construction, Reconstruction, Maintenance, Protection of Highways, Regional Roads, and Procurement of Equipment and Devices for the Needs of Roads or Road Objects (OG of RS, no.25/99) (hereinafter called RS Roads Regulations) is also in force. Like the RS Buildings Construction Rules, the RS Roads Regulations are very general in nature and lacking in procedural detail.

A notable difference between the two instruments is that the RS Roads Regulations provide, in addition to public tender, a procedure involving an open call for prequalification followed by a collection of bids from prequalified bidders. By contrast, the RS Building Construction Regulations mention the competitive tendering method as the general norm, with the exception of a Direct Solicitation method for procurement estimated to cost less than 400,000 YuD (US$6,200).

The usefulness of these instruments to Serbian public procuring entities has been substantially reduced, because the effects of high inflation since their enactment, have drastically lowered the thresholds as to render them unworkable.

These enactments constitute a wholly inadequate set of provisions for the conduct of public procurement in Serbia. They fail to provide a clear, comprehensive set of rules for awarding public contracts, afford almost unlimited discretion to public officials in making decisions about procurement and lack even the most basic elements of transparency, competitiveness and accountability found in other, more developed bodies of procurement legislation, for example those of Poland or Hungary. To its credit, the Serbian Government, responding to accusations of corruption and driven by the desire for closer economic integration with the EU, has already taken steps to draft a new draft Public Procurement Act. The World Bank's comments on the draft Serbian Public Procurement Act are provided at Annex G to this report.

Republic of Montenegro: The legislative legacy of both the SFRY and FRY on public procurement has been swept aside by the enactment, in August 2001, of a new Law on Public Procurement of the Republic of Montenegro (hereinafter called the RM Procurement Law).

The RM Procurement Law is built on sound principles and deals with all of the provisions which one would expect to find in a modern procurement law, including a reasonably wide range of procurement methods, including two-stage tendering, negotiated procurement and shopping, the establishment of a central policy and monitoring body, and the provision of a bid protest procedure. However, the law is cumbersome, containing many, detailed provisions which resemble bidding instructions, and with a confusing ordering of provisions. For example, provisions on contract administration are contained in the clauses related to instructions to bidders. One telling measure of the complexity of the law is that, from its adoption in August 2001 until May 2002, the Public Procurement Commission has been required to publish 210 legal opinions clarifying the application of the law.

The Government of Montenegro considers the RM Procurement Law to be fully consistent with the Procurement Directives of the European Union (EU), an important step for reaching its goal of economic integration with Europe.

C.1.4 Scope of Application of Legal Enactments

At the Federal level, the various enactments listed above apply to procurement conducted by all Federal state institutions, which include fourteen Ministries and some thirty other institutions.

At the RS level, the scope of current enactments, based on the Law on Assets in the Property of Republic of Serbia, encompasses state bodies and organizations, bodies and organizations of territorial autonomy and local self governments, public services (public companies and institutions) and other organizations the founder of which is the Republic of Serbia or one of its territorial units.

The draft RS Procurement Act applies to government agencies, organizations and institutions or compulsory social insurance organizations, legal entities founded by a direct or indirect budget beneficiary, where more than a half of their management or shares belong to budget beneficiaries and public enterprises and their affiliated companies in which a direct or indirect budget beneficiary holds a majority share.

The RM Procurement Law applies to ministries, departments, secretariats, courts, local self-governments, to any public entity which derives public funds for public procurement, as well as to Government-owned companies, entities and firms which are not financially autonomous from the Government.

C.1.5 Public Accessibility of Legal Texts

Neither public officials nor the general public enjoys sufficient access to legislation. Under the Milosevic regime, the Government adopted many decrees, some of which were never made public. The Government also did not have the resources to consolidate or revise the proliferation of laws and regulations as they were issued, thus accruing a backlog of unconsolidated legal texts. Given their strained financial condition, the current Federal and Serbian governments still lack the resources to publish new laws systematically. As a result, many public officials in the Federation and Serbian Governments are unsure of the laws and sub-legislative enactments which govern procurement.

In Montenegro, by contrast, awareness of the new Law on Public Procurement was found to be high because Government had accorded the law high priority, and there had been a full public debate on the law when it was in draft form.

The Government of Montenegro recently launched a website called Public Procurement in the Republic of Montenegro (www.nabavka.cg.yu), where it publishes current legislation electronically in both local and English languages. The Government of Serbia has recently declared its commitment to launch an "Open Government" by publishing all of its documents on the Government Internet website (www.serbia.sr.gov.yu), starting in January 2002. This development, if fully implemented, should substantially improve the accessibility of legal texts related to public procurement and to other areas of law.

A list of the Federal, Serbian and Montenegrin laws reviewed for this report is found in Annex C.

C.2 Procedures, Practices and Application

This section provides a step-by-step commentary on the practical application of the laws and regulations to the procurement process, from procurement planning through to contract administration, and highlights how the weaknesses of the current enactments regularly show through in bad procurement practices. This assessment is based on interviews conducted during the assessment and on responses to detailed questionnaires on procurement operations distributed as part of the assessment.

C.2.1 Procurement Planning

The challenge of instituting proper procurement planning faces a number of hurdles, some of which are historical and others which are the result of poor organization and practices. First and foremost, project approval and planning are currently in transition from the past regime, where approvals to spend public funds, particularly on high-value capital projects, was often hijacked by special interest groups with close connections to the political elite, to a more formal and economically rational approach. Practices redolent of the old ways continue and periodically feature in press accounts in Serbia. For example, one recent article reports on a high-value procurement of automobiles undertaken by a ministry using a "fast track" procedure, as a result of which contracts were placed with two foreign manufacturers without the benefit of competition.

The RM Procurement Law and the draft RS Procurement Act require the procuring entity to ensure that adequate budgetary appropriation has been secured before initiating a procurement. However, this provision offers only a partial solution to the many problems which currently make procurement planning both inefficient and ineffective. These problems include the chronic weakness of public institutions, poor coordination between actors in the planning process and a lack of clarity about their roles, underdeveloped planning capacity, a decline in government services that support procurement planning (for example, the inadequacy of official statistics contributes to the preparation of inaccurate cost estimates), and the vulnerability of the planning process to corruption.

A salient example of many of these problems is provided by the health sector. Several public hospitals in Serbia have conducted tenders — for example, for the procurement of medical consumables—without first having a budgetary allocation for the purchase in place. They have then signed a contract with the winning bidder and sent the supplier's invoice to the RS Health Insurance Fund (HIF), which is then obliged to pay it, even though it has not been consulted on the requirement and has no control over the specification of the products, the prices paid, or the intended use of the supplies procured. In other cases, Serbian procuring entities have placed contracts for the supply of pharmaceuticals and medical supplies without knowing the actual needs of healthcare institutions or the existing stock levels. It later transpired that the same products had been procured simultaneously through external humanitarian assistance, resulting in over-supply of certain items, while other pressing requirements went unmet. A further example of poor planning is the policy of the Montenegrin health authorities to purchase only brand-name pharmaceuticals, when acceptable generic products are widely available on the international market at significantly lower prices.

C.2.2 Assessment of Bidders' Qualifications and Other Participation Issues

The assessment learned of many problems in the assessment of bidders' qualifications, such as a lack of clarity in bidding documents regarding the specific qualifications required for a particular tender and unclear definition of the reference documents required to be submitted by bidders. This has resulted in an excess of discretion being placed in the hands of procuring entity officials, the unnecessary rejection of good bids and the award of contracts to unqualified bidders. The correct application of appropriate qualification requirements in public tendering is particular important in Yugoslavia now, given the weakened state of many of the companies which bid on Government contracts. A relevant example is the construction sector, where years of under-investment have diminished the technical and financial resources of most local contractors.

The draft RS Procurement Act relies heavily on the EU Procurement Directives in their formulation of provisions on the treatment of bidders' qualifications (technical, financial and eligibility criteria), indications of the type of documentation to be submitted by bidders to evidence their financial and technical qualifications, and safeguards to ensure that the qualification assessment process does not create obstacles to participation by foreign bidders. The draft RS Procurement Act also combines into the Restricted Procedure procurement method a pre-qualification stage in all cases where that procedure is used.

The draft RS Act also contains provisions on establishing lists of pre-qualified bidders; the application of such lists is mandatory for the award of contracts in four utilities sectors – water, energy, telecommunications and transport - a concept similar to the EU Utilities Directive. Consideration might be given to measures, such as updating the list frequently, to ensure that the lists do not exclude new, qualified applicants from being added at any time.

In the absence of pre-qualification, the use of post-qualification is provided for in both the RM Procurement Law and the draft RS Procurement Act, though the clarity of the provision in the draft RS Act may be diminished by another provision which provides that post-qualification be applied to all bidders, not just the bidder recommended for award of contract.

C.2.3 Participation by Foreign Bidders and Application of Domestic Preference

Although neither the RS Building Regulations nor the RS Roads Regulations clearly establishes a principle of non-discrimination against foreign bidders nor contains any provisions on the application of a price preference scheme to domestic bidders, both are in fact practiced. Indeed, the assessment noted instances where local authorities apply preferential policies to bidders based on their localities, thus discriminating against other national bidders from different parts of the country.

By contrast, both the draft RS Procurement Act and the RM Procurement Law affirm the principle of non-discrimination and equality of participation. However, in some of their detailed provisions, both instruments subtract from this general principle. For example, the draft RS Procurement Act envisages that another law or an international agreement may require preferential hiring of specific national sub-contractors and leaves the door open to the subsequent passage of regulations which would involve the determination of the specific origin of goods and services, presumably Yugoslav, or perhaps even Serbian, sources. In addition, in the utilities sector, the draft RS Act provides that discrimination in favor of domestic bidders is permissible when they are in competition with a bidder from a country with which the FRY does not have an agreement on reciprocal access for Yugoslav bidders to that country's public market.

The RM Procurement Law distinguishes between Open International Competitive Bidding and Open Local Competitive Bidding and between Limited Local Competitive Bidding and Limited International Competitive Bidding, with both local variants being open only to local bidders.

Foreign suppliers, contractors and consultants are permitted to operate in the FRY according to the Law on Foreign Investment, the Law on Foreign Trade Transactions and the Law on Concessions. They may do so either by having a corporate establishment in FRY (under the Law on Foreign Investment and the Law on Concessions), or on the basis of a trade contract with a foreign contractor (under the Law on Foreign Trade Transactions). The latter law provides that foreign contractors may perform construction works awarded by public tender, provided they engage Yugoslav labor, although the management may consist of foreign personnel.

The process of establishing a company is generally complicated and time-consuming, due to the multiplicity of formalities and approvals required, a situation which almost certainly has a greater adverse effect on foreign investors than on local ones (see also Commercial Regulations below).

While neither the draft RS Procurement Act nor the RM Procurement Law contains any provision for a price preference in favor of domestic bidders, the draft RS Act provides that bids for services contracts in the utilities sector whose prices are within 3 percent of each other may be deemed to be equivalent in price. This unusual provision, the justification for which is not clear, may be applied in a manner which affords preference to local bidders and, certainly, unnecessary discretion to the decision-maker.

C.2.4 Minimum Number of Bids Requirement

The submission of a minimum of three bids is required by both the RS Building Construction Regulations and the RS Roads Regulations, absent which the procuring entity may repeat the tender on the same or changed terms and conditions. The concept of a minimum number of bids is retained in the draft RS Procurement Act, but the required number is reduced to two. Failing receipt of two bids, the RS draft Act allows the procuring entity to proceed on the basis of the Negotiated Procedure. The RM Procurement Law, by contrast, has no rule on minimum participation.

C.2.5 Procurement Methods

The three main legislative enactments currently in force in FRY, two in Serbia and one in Montenegro, plus the draft RS Law, differ widely in procurement methods. While it is intended that the RS Buildings Construction Regulations and the RS Roads Regulations will disappear when the draft RS Procurement Act becomes law, nonetheless they are reflected in this report, as they are in force at the time of writing and, therefore, still govern current procurement operations.

The RS Buildings Construction Regulations and RS Roads Regulations both provide a competitive tendering method. In addition, the RS Buildings Construction Regulations includes a “collection of tenders” method, equivalent to restricted tendering, which must be preceded by a pre-qualification stage based on open solicitation of applications to pre-qualify. The RS Roads Regulations feature a similar method for lower-value contracts for goods and works less than YuD 400,000 (US$6,200) in value.

Table 2: Available Procurement Methods under Current and Draft Legislation

Current Legislation			Draft Legislation
Serbia		Montenegro	
RS Buildings Construction Regulations	**RS Roads Regulations**	**RM Procurement Law**	**Draft RS Procurement Law**
Competitive Tendering Restricted Tendering (after pre-qualification)	Competitive Tendering Direct Solicitation	Competitive Bidding (local or international, limited or open) Two-stage Bidding (local or international, limited or open) Request for Proposals Shopping Direct Agreement	Open Procedures Restricted Procedures Negotiated Procedures

The RM Procurement Law

The RM Procurement Law presents a full range of procurement methods but is rather unclear as to whether Open Competitive Bidding is the priority method. This lack of clarity leaves room for additional discretion by the procuring entity. It also draws a distinction between national and international versions of competitive bidding, both in its open and limited forms. The RM Law seems to distinguish, though rather unclearly, between a version of limited competitive bidding with pre-selection (i.e., the drawing up of a list) and a version with pre-qualification proceedings. Both versions entail publication of a notice.

It would appear that the RM Law has taken a more restrictive approach to negotiated procurement than the draft RS Act, patterned more on the UNCITRAL Model Law approach to single-source procurement, while still meeting the minimum standard set in the EU Directives. The RM Law considers emergency situations as exceptional grounds, subject to documenting of the need for acceleration, for the use of the direct agreement method. In addition to other grounds mentioned in the Law, direct agreement is permitted for very low value contracts (below a DM 1,000 per contract threshold, as set by decree).

The RM Law provides a Shopping method of procurement for a variety of different cases. Monetary limits per transaction have been set by decree for various of those situations:

- small commodities under DM 5,000 per purchase order;
- where the value of the purchase order for any item is under the prescribed amount (DM 10, 000 per purchase order and, DM 2,000 for any item);
- standardization of goods;
- leasing by shopping.

Unlike the draft RS Act, the RM Law includes a Request For Proposals method, especially for procurement of consultant services. The text addresses various aspects of such a procedure, including the terms of reference; drawing up of the three to seven candidate shortlist, with an

advertising procedure to invite expressions of interest for contracts estimated to be above a prescribed level; selection methods available (e.g., "quality- and cost-based" or "quality-based" selection); criteria and methodology for evaluation and comparison of technical and financial proposals; negotiation process leading to contract proposals; and prohibition against hiring of consultants in a conflict of interest position with regard, for example, to previous or current other assignments.

By contrast, and in line with existing practice, the draft RS Act subjects procurement of consultants' services to open tendering as the norm, unless such a procurement meets the criteria for the use of restricted tendering or a negotiated procedure.

Procedures to be applied in the open and limited forms of competitive bidding are generally. sufficiently described in the draft RS Act and the RM Law. In fact, at some points the RM Law presents so much detail that the instrument takes on the character of instructions to bidders rather than that of a law.

Draft RS Procurement Act

The approach taken in the draft RS Procurement Act by and large replicates the EU Procurement Directives, although, by stating that the Open Procedure is to be used, it exceeds the minimum standard set in the EU Directives, which substantially leaves the choice between the Open and Restricted procedures to the procuring entity, provided that the required advertisement procedures have been followed.

The Restricted Procedure is available only when there are only a limited number of suppliers, for standardized purchases that could not be planned for ahead of time. In fact, the holding of pre-qualification proceedings is an indispensable first step in every use of the Restricted Procedure.

The draft RS Act includes a Negotiated Procedure, modeled closely on the negotiated procurement method included in the minimum standard for procurement methods to be met by countries in which the EU Directives apply. Restricting resort to negotiated methods of procurement will be a challenge in the FRY, given the widespread practice of awarding contracts on the basis of negotiations and non-technical factors.

As do the EU Directives, the draft RS Act lumps together in the negotiated procurement method cases in which there truly is only one possible supplier with cases in which there are two or more possible suppliers.

The draft RS Act mirrors the conditions for use of the Negotiated Procedure found in the EU Directives. Accordingly, when the Negotiated Procedure may be used will differ depending upon whether it will be conducted with a prior notification to bidders or without a notice. Negotiation procedures without prior publication of a notice are permitted in the following cases:

(i) no tenders or no responsive tenders were received in a prior open or restricted procedure;
(ii) the procurement need can only be fulfilled by a limited number of suppliers (not included in the RM Law), or in case of emergency (in these two cases, approval of the Public Procurement Office is required);
(iii) extension of the scope of existing supply or works contracts, or repetition of a works contract (the draft omits the EU three-year cap for supply contract extensions of this type, perhaps inadvertently, but does replicate the EU cap of 25 percent of contract value for contract extensions and the three-year window from the date of conclusion of the original

contract for repeat works contract, subject to mention of repeat possibility in the original solicitation); and

(iv) research contracts not entailing commercial production.

A Negotiated Procedure with prior publication of a notice is envisaged, for example, when the nature of the procurement or the performance risk does not permit fixing of total price at contract formation and when, in a prior open or restricted procedure, inadequate or unacceptable tenders were received, provided that all bidders who had submitted bids in the preceding proceeding are invited (not included in the RM Law) and there is no substantial change in bidding documents.

In the case of services, use of the Negotiated Procedure with prior publication of a notice is also permitted by the draft RS Act when the nature of the services (particularly a specified category of intellectual and financial services) is such that the technical description of the services cannot be established with sufficient precision to use the open or the restricted procedure.

While the approach of providing such a ground only in the case of services is in line with the existing EU Directives, the draft Consolidated Directive currently being prepared by the EU provides this type of ground for the use of negotiated procedure, in the form of a new two-stage procurement method not unlike two-stage tendering in the UNCITRAL Model Law, to other types of procurement. In the RM Law, for example, there is a "two-stage bidding" method available to be utilized for large, complex, high-technology type of procurement of goods or works.

Also noteworthy is the manner in which the draft RS Act, following the EU Directives, provides expanded possibilities for use of the negotiated procedure without prior publication in the utilities sector.

Both the RM Law and the draft RS Act provide design contests as an adjunct to the procurement process, but the provisions in the respective texts differ somewhat. For example, the draft RS Act describes the requirements for an independent jury and for anonymity of participation in the contest, neither of which is mentioned in the RM Law. Aspects addressed in the RM Law include only the copyright in the design, pre-approval of holding of the design contest by the Pre-Investment Committee, and contents of the advertisement.

The draft RS Act suffers from a limited range of procurement methods which may cause problems with the application of the laws. Following as it does the EU Directives, the draft RS Act has no procedure like shopping for lower-value procurement. It does, however, call upon procuring entities to establish their own internal regulations for awarding low-value contracts, and establishes a six-month window following entry into force of the draft Act during which the Government may issue uniform regulations governing low-value procurement. While the draft Act lists the issues to be addressed in such procedures, it does not provide essential minimum standards. Minimum standards are especially important where most procuring entities lack capacity and are affected by corruption.

C.2.6 Invitations to Bid

Both of the existing regulations in Serbia require the publication in the Official Gazette of an advertisement, which may be either an invitation to tender or a call for "open competition for qualification." The regulations also list the required contents of the advertisement, which may include the procuring entity's cost estimate for the procurement requirement, a disclosure which may facilitate collusion among bidders.

The draft RS Procurement Act requires publication in the Official Gazette of all procurement notices, including invitations to bid. Patterned on the EU Directives, the draft Act provides a greater variety of notices in the run-up to a procurement proceeding, combinations of which can result in a reduction of the bid submission period. The range of notices includes:

- a prior notice, to be published within a year of a procurement exceeding the level set in the Act. In the utilities sector, that notice is linked to a restricted or negotiated procedure; and
- a periodic indicative notice.

The time limit for submitting a request to participate in response to an announcement in a restricted or a negotiated procedure with a prior publication of a notice is 25 days.

The RM Procurement Law requires publication of a notice of invitation in the case of Open Competitive Bidding, and, in the case of Limited Competitive Bidding, a notice of the pre-selection procedure. For consultancy contracts exceeding the level set by decree at DM 50,000 in preparing the short list, publication of a notice seeking expressions of interest is required, with a 30-day period to respond. While provisions on advertising are specified in the RM Law, it does not specify the place of publication, which suggests that the present practice of publication in newspapers will continue. Montenegro has also taken the progressive step of launching a website dedicated to public procurement, on which invitations to bid are required to be advertised (www.nabavka.cg.yu). From its inception in February, 2002 until May, 2002, 160 tenders have been advertised on the website. No such initiative has yet been taken in Serbia, though this step should be part of the comprehensive overhaul of the public procurement system in the Republic, of which the enactment of the draft RS Act is the first component.

C.2.7 Bidding Documents

The use of standard bidding documents has not been widely practiced in the FRY. The RS Roads Regulations refer to informing bidders of the manner of purchasing bidding documents and provide that only bidders who have purchased the bidding documents may submit a bid, but they do not set any minimum contents for the bidding documents. The RS Building Construction Regulations do not even go that far, referring only to a determination by the procuring entity as to "the place and time for acquainting" bidders with details of the procurement. The lack of standard procurement documents reinforces various undesirable practices, including lack of clear instructions to bidders on the preparation of their bids; failure to provide the terms of the eventual procurement contract in advance of bid preparation ; inadequate pre-disclosure of bid evaluation criteria or no ranking or weighting of the criteria, in cases where they are given; frequent conduct of procurement proceedings without the use of bidding documents.

The draft RS Act contains more developed provisions which require the preparation of bidding documents and list the required contents of those documents, including a "model contract." They require the preparation of the documents in Serbian, with the possibility of additional foreign language versions.

In Montenegro, a set of standard procurement documents was prepared in parallel with the drafting of the new law, but they are not yet in widespread use and it seems inevitable that public officials will need substantial training and familiarization in their use before they can be expected to have the desired outcome of increasing correct application of the law.

C.2.8 Bid and Contract Price and Currency

The RM Law requires the bidding documents to indicate the currency or currencies in which bidders may state their prices and the procedure for comparing bids quoted in different currencies. It also permits contracts to be priced in a variety of ways: lump-sum, unit price, turnkey, cost-plus or provisional price. Price revision also is mentioned with respect to supply of spare parts for equipment over a period of time. The draft RS Act requires values stated in bidding documents and in bids to be expressed in Dinars, though the bidding documents may request that bidders state values also in other currencies and may permit bids to be priced in other currencies. The draft RS Act makes no reference to price revision in contract clauses or otherwise.

Price controls may be applied pursuant to both federal and republic laws, such as the FRY Law on Social Price Control. The federal government is authorized to apply price controls in certain circumstances and in the case of "goods and services of interest to the country as a whole." The effect of such provisions on prices in contracts will not be tested until the draft RS Act comes into force. In Montenegro, where the Procurement Law has been in effect since August 2001, Federal price control provisions appear to have no effect on prices in contracts placed under that law.

C.2.9 Bid Preparation and Submission

The current RS regulations contain partial provisions on bid preparation and submission, which provide that tenders must be submitted in writing and in a sealed envelope. Both sets of regulations provide for a truncated 15-day period for bid preparation, which is wholly inadequate in terms of transparency and promoting competitive participation by bidders. This period is expanded upon in the draft RS Act, which sets a minimum period of 40 days from the date of publication of the invitation to tender in an Open Procedure. However, that period may be reduced to 30 days or even 22 days in the event that a prior notice about the procurement has already been published. The time period is calculated from the date of the publication of the invitation, rather than from the date of the availability of bidding documents, which would be a more transparent provision.

The RM Procurement Law lays down the principle that the period for bid preparation should be determined taking into account the nature of the procurement and refers to a prescribed minimum number of days. For local tenders, the period allowed for preparation of bids runs from a minimum of 7 days to a maximum of 24 days; for international tenders, the minimum period is 24 days and the maximum 84 days. At the lower end of this range, the periods allowed are clearly too short. To promote fairness, transparency and competitiveness, bidders should be allowed at least 30 days for bid preparation.

C.2.10 Bid and Performance Securities

Neither the RS Buildings Construction Regulations nor the RS Roads Regulations make any mention of bid, performance or any other type of securities. The draft RS Act requires that the bidding documents disclose the bid security requirement and illustrates acceptable forms of such security, a formulation that might be read as an across-the-board requirement of bid securities. It does not, however, define supplemental aspects, such as the circumstances in which a bid security may be encashed. The RM Procurement Law provides more detail about the use of securities in the procurement process, in that it mentions not only bid securities but also performance securities, advance payment securities and retention money.

C.2.11 Bid Validity Periods

The RM Procurement Law establishes the need to specify a bid validity period, calling for sufficient time to allow evaluation of bids and obtain any necessary approvals; it also allows the procuring entity to seek voluntary extensions of the validity period. None of the RS instruments, current or draft, mentions bid validity or its attendant issues.

C.2.12 Bid Opening

Both the RS Building Construction Regulations and the RS Roads Regulations provide for opening of bids in the presence of bidders or their representatives. However, those provisions call upon the evaluation committee to carry out a number of steps which go beyond bid opening and trespass on the territory of examination of bids, such as checking bids for responsiveness and completeness, eliciting comments of bidders on such findings and rejection of bids. These untransparent provisions appear to lie at the root of the many reports from bidders of unfair rejection of their bids at bid opening.

The draft RS Act provides for a written summary of the bid opening to be prepared, and is, for the most part, more in line with generally accepted practice. Worrisome aspects, however, include a provision that permits the procuring entity to waive public opening on the grounds of protecting a potentially wide range of secrets, including not only military, but also trade, official or state secrets, and another that envisages an "anonymous invitation to tender" pursuant to which the names of bidders are not revealed. It remains to be seen how such loose provisions, which seem open to abuse, will be applied in practice when the Act comes into force.

The main provisions on bid opening in the RM Law include the establishment, composition and functions of the Opening Committee and public opening above a defined threshold of DM 60,000, as set by decree. In one key aspect, the RM Procurement Law is superior to the draft RS Act, in that the former affirms that the time for opening of bids should coincide with the deadline for the submission of bids, a key element of transparency which is absent from the draft RS Act.

C.2.13 Evaluation and Comparison of Bids

The crucial area of the evaluation of bids and selecting the winning bid is one of the most untransparent aspects of procurement practices in Yugoslavia. The factors which contribute to these difficulties include:

- repeated budget shortfalls which lead procuring entities to accord insufficient importance to price as the overriding evaluation criterion in the procurement of goods and works and to emphasize, instead, bidders' willingness to offer deferred payment terms;
- the absence, in most cases, of a clear evaluation procedure;
- the widespread use of opaque and subjective evaluation systems, including merit point systems in which the weighting scheme is neither defined in advance, nor communicated to the bidders. This practice gives decision-makers unrestrained latitude in the treatment of bids under evaluation and further exaggerates the already excessive discretion afforded public officials under the legislation itself;
- the inadequate technical description of procurement requirements in the bidding documents, which inhibits fair comparison of bids;
- the use of bidders' qualifications and references as comparative criteria in the evaluation of bids, rather than as part of pre-qualification or post-qualification;

- allowing bidders to examine each other's bids, which represents an inappropriate breach of confidentiality and compromises fair competition;
- inappropriate contacts between bidders and high-ranking officials after bid opening and prior to the award decision.

The recent enactment of the RM Procurement Law and the current preparation of the draft RS Procurement Act present an invaluable opportunity to eliminate these and other abusive practices. Both instruments contain improvements, such as requiring pre-disclosure of the bid evaluation criteria in the bidding documents and the rejection of late bids. Both instruments also make provision for the application of price, price-related and non-price criteria.

Apart from those basic similarities, there are some differences in the approaches of the two texts. For example, the draft RS Act requires that, in the Restricted Procedure, which is preceded by pre-qualification, the evaluation of bids should be based solely on lowest price.

The RM Procurement Law introduces the notion of responsiveness of bids and draws a useful distinction between major and minor deviations, an important distinction for preventing the unnecessary or abusive rejection of bids. By contrast, the draft RS Act does not mention the concept of a range of responsiveness, setting forth instead three categories into which bids may fall that are not readily distinguishable or understandable: "correct tender", "appropriate tender" and "acceptable tender." Such unclear distinctions fail the key test of transparency in bid evaluation and look certain to lead to a continuation of errors and abuses in the handling of bids during evaluation.

The RM Procurement Law establishes procedures for the evaluation of proposals for services, provisions not found in the draft RS Act, as it does not provide a special method for the procurement of services. The draft RS Act provides a procedure for dealing with abnormally low bid prices, a matter not addressed in the RM Law. Both texts set forth a rule barring negotiation in the evaluation process. However, the clarity of that rule's application is substantially diminished in the draft RS Act by the presence of negotiated procurement procedures.

C.2.14 Conclusion of Contract

The practice of negotiating contract terms after the award of the contract appears to be widespread in Yugoslavia and is facilitated by the routine practice of not including the contract terms in the bidding documents. In the presence of a high level of procurement-related corruption in the country, the frequency of negotiation introduces an unacceptably high risk that bribes may be demanded and paid when public officials engage in negotiations with bidders.

C.2.15 Notification of Contract Award

Whereas the draft RS Act requires publication of all awards in the RS Official Gazette within 14 days of the award, with the time period relaxed to 48 days in the case of award of services contracts, the RM Procurement Law requires published notices of award only for contracts above a threshold of DM 200,000, a less transparent provision. The RM Law requires procuring entities to submit information on contracts below this threshold to the Public Procurement Commission, which, in turn, is to publish, at least once a year, compilations of information on contracts awarded.

The draft RS Act obliges the procuring entity to give notice, with justifications for award, to the winning bidder and all other bidders on the award of contract. The same obligation lies on the

procuring entity in case of non-qualification in a pre-qualification procedure. Individual notices of contract award specifically to the winning bidder is required by the RM Law, but has been omitted in the draft RS Act, as it had been in the RS Building Construction Regulations and the RS Roads Regulations. The draft RS Act provides for debriefing to bidders whose bids have been rejected, a valuable boon to transparency and accountability not found in the RM Law.

C.2.16 Record of Procurement Proceedings

The RS Buildings Construction Regulations and the RS Roads Regulations contain provisions requiring the recording of information on procurement proceedings, which require the Tender Committee to prepare a protocol describing various aspects of the bid opening and preliminary examination stages. In addition, the Committee must prepare a bid evaluation report, which must be presented to the competent authority. Provisions on recording and archiving appear in various places in the draft RS Procurement Act, reflecting the generally fragmented structure of that instrument. These require the procuring entity to maintain records of all phases of a procurement proceeding, through the execution of the procurement contract, and to retain the related documentation for a prescribed minimum period of time. In addition, the draft RS Act refers to the preparation of minutes of the bid opening, which are to be delivered to bidders that have submitted bids, as well as a report on the award of the contract. Apart from the distribution of the minutes of the bid opening, no mention is made in the draft RS Act of any required disclosure of the records.

Related provisions in the RM Law address the report of the bid opening, evaluation reports, archiving and availability to the general public of Award Committee minutes and an obligation to record and safeguard all relevant documents. Those provisions, however, are vague as to whether the procuring entity is required to maintain a record of the decisions and actions taken at key stages of the procurement proceedings.

C.2.17 Contract Administration and Management Resources

Both experience and expertise on contract administration is in short supply in Yugoslavia, given the recent shortage of major capital investments by the public sector, whether financed by domestic or external sources. Given that the country has only recently rejoined the World Bank and become a member of the EBRD, experience gained in managing contracts funded by those and other international institutions remains very limited.

In Serbia, neither the RS Buildings Construction Regulations nor the RS Roads Regulations sets any specific standard for contract administration. The draft RS Act is similarly silent on the issue. By contrast, the RM Procurement Law includes provisions restricting variations to those envisaged in the contract or permitted as an extension of the contract under the provisions on direct agreement. It also clearly establishes the responsibility of the procuring entity for works supervision, with the possibility of obtaining outside assistance from the RM Department of Public Works, which conducts both civil works procurement and construction supervision on behalf of Montenegrin public bodies, or from a consultant.

C.2.18 Implementation Delays

Implementation delays stem from a variety of factors, including weaknesses in the supporting institutions, characterized by lack of capacity and time-consuming administrative processes which require multiple approvals, notifications, registration, fees, and excessive administrative discretion, for example to obtain licenses and permits. Other significant sources of delay include

arbitrary, inefficient and time-consuming customs procedures, multiple layers of inspection, protracted contract negotiations, a result of not including a sample contract in the bidding documents, the absence or paucity of advance payments to works contractors, which reduces the ability of already cash-strapped firms to bear the cost of timely and efficient mobilization.

C.2.19 Quality Control

The FRY has inherited extensive experience and developed institutional mechanisms in the area of technical standards. The national standards bodies, the Standardization Institutes (federal and Serbian) enjoy membership in the International Standards Organization (ISO) and in International Electrotechnical Commission (IEC), and is associated with the European Committee for Standardization (CEN) and the European Committee for Electrotechnical Standardization (CENELEC). In addition, the Yugoslav Accreditation Body (YUAT) has been established to accredit laboratories and certification bodies. The operation of the FRY standards system, once renowned as one of the best in Eastern Europe, has suffered in the past decade. Of the 13,000 or so national standards in place, many were, upon issuance, identical to or aligned with international standards. With the passage of time, they have become outdated, a factor which has given rise to the direct use of international standards in purchasing. Some 300 regulations have been issued to implement the standards, but many of them are also outdated. Prior to 1996, the issuance of technical regulations to implement the standards was under the purview of the Standards Bureau. Since then, the issuance of regulations has virtually ground to a halt, thus leaving significant areas uncovered or subject to outdated regulations and resulting in technical barriers to trade. An internal expert group has been established to facilitate the transition of standardization in the FRY and a new standards law is being prepared.

Imports, including those for public procurement purposes, are subject to a scheme for quality inspection and attestation or certification. That process is hampered, however, by inadequacies in existing laboratory facilities.

C.2.20 Payments

Chronic budgetary shortfalls result in perennial payment delays. Such delays not only impact negatively on the operations of suppliers, in particular small businesses, but also discourage their participation in public procurement proceedings. As noted above, payment considerations also distort the contract award process, by forcing procuring entities to utilize the financial resources of bidders as one of the key criteria in the evaluation of bids. Preference is given to bidders who are able to forego advance payments and sustain deferred payment, sometimes of more than one year. In this respect, public institutions habitually subcontract their illiquidity problem to often reluctant bidders who, despite their own lack of liquidity, are left little choice but to accept these unfavorable terms, if they are to win a scarce public contract.

A statutory interest rate for late payments is stipulated by law, so such a provision does not need to be included in contractual agreements. This rate is calculated based on the monthly statistical increase of retail prices, increased by a monthly margin of 0.5 percent.

The shortage of liquidity has spurred the use of barter and compensation, in particular for offsetting suppliers' tax arrears, as a substitute for cash payment of contract prices and arrears.

C.2.21 Bid Protests

While some procuring entities may have informally entertained complaints from bidders, there has until recently been no formal mechanism in place in Yugoslavia specifically tailored to administrative review of complaints from bidders alleging injury due to violations of procurement procedures. This deficiency is set against a backdrop of general inadequacy in the procedures available for review of administrative decisions. For example, while the FRY Law on Administrative Disputes (1996) provides for appeal and review of administrative decisions and settlement of disputes, and while the FRY Law on Administrative Procedures (1997) sets time periods for the issuance of administrative decisions, that process remains inefficient and inadequate for the specialized needs of the public procurement process. There is also a cultural phenomenon at work in Yugoslavia, as in other former constituent republics of the SFRY, by which the rights of the state are widely perceived to take precedence over those of the individual citizen. The effect of this perception is an abiding reluctance on the part of persons, both natural and legal, to submit a formal complaint against the actions of a public institution.

A first attempt at establishing an administrative review procedure is enshrined in the RM Procurement Law, which charges the Public Procurement Commission (PPC) with investigating complaints from suppliers and proposing remedial action. However, this is a limited reference that falls short of establishing a legislative framework for an effective bid protest system. Given the recent establishment of the PPC, it is perhaps unsurprising that the bid protest mechanism in Montenegro is still not working entirely satisfactorily for a number of reasons, primary among them the fact that bidders are unaware of their rights or of how to go about asserting them. Nevertheless, in the period January- June 2002, eleven appeals were submitted to the PPC, of which seven were upheld and four rejected. In the four cases where the protest was upheld, the PPC nullified the bidding process and ordered the tender to be repeated. Although there have been some reports of reluctance on the part of the affected public procuring entities to heed the PPC's instruction, all have eventually done so, when faced with the prospect of earning a mention in the PPC's annual report to Parliament.

In Serbia, the draft RS Procurement Act requires that, in the case of procurement with a value exceeding YUD 300 M (US$4.65 M), a copy of the bid should be submitted to the institution charged with external audit of public expenditures. Pending the initiation of activities of the institution charged with such external audit, the Government has the discretion to engage the services of independent auditors. These provisions do not constitute a functioning bid protest system.

C.2.22 Environmentally Responsible Procurement (ERP)

Current legislative enactments and practice of public procurement in Yugoslavia make no mentions of the environmental aspects of procurement. Given this gap, governments at all levels are missing a valuable opportunity to use their considerable purchasing muscle to promote sound environmental policies, such as requiring public purchasers to give preference, when making purchasing decisions, to environmentally sound equipment at the expense of alternatives which may pollute or which may carry high costs for decommissioning or disposal. Given the environmental challenges which face Yugoslavia, this is an area of procurement policy to which governments should pay attention in the future.

C.3 Organization and Resources

This Section looks at how responsibility for the conduct and oversight of public procurement is apportioned to the various institutions at different levels of administration in FRY and reviews how oversight functions are being performed.

C.3.1 Organization of the Procurement Function within Public Institutions

At the federal level and in Serbia, procurement proceedings are generally conducted by a Tender Commission, comprising a membership of three to five officials nominated by the General Director of the institution. Membership usually includes a lawyer and, for civil works contracts in Serbia, a member of staff from the Ministry of Urban Planning and Construction. However, as presaged by the provisions of the RS Roads Regulations highlighted above, there is wide variability in the role of Tender Commissions in different institutions and their authority to make decisions about procurement is undermined by the discretion which the legislation affords the General Director.

Staff of major purchasing institutions interviewed for this assessment recounted that, while the Tender Commission evaluates the bids and, in some cases, proposes the winner, the actual decision on award is entirely at the discretion of the General Director, who is at liberty to overturn the recommendation of the Tender Commission. In other cases, the Tender Commission merely analyzes the bids for general compliance, without ranking them or making any specific award recommendation and, again the decision on the award of contract is left to the General Director. Yet another variation is that the Tender Commission identifies the "best" three bids and presents those for the Director for him to make the award decision. In making his decision, the General Director is entirely free to award the contract to one of the three "best" bids identified by the Tender Commission or he may bypass those three bidders and award the contact to any other bid among those submitted.

In summary, while current practices vary widely between different procuring entities, the one characteristic which they share is opacity.

By contrast, the RM Procurement Law contains extensive provisions defining the authority and responsibility of both Public Procurement Officers and of Evaluation Committees. For Direct Agreement and Shopping procurement methods, the Public Procurement Officer is solely responsible for the conduct of procurement proceedings, including evaluation of bids. In all other procurement methods, the procurement process is split between an ad hoc Opening Committee, comprising three people, and an Evaluation Committee, comprising a supervisor and three to five evaluators, all of whom are appointed by the head of the procuring entity. Members of the Opening Committee may not subsequently serve as members of the Evaluation Committee for the same procurement. The Law clearly establishes that the recommendation for award of contract made by the Evaluation Committee cannot be overturned by the procuring entity.

C.3.2 Basis of Accountability of Public Officials

One of the most egregious legacies of the previous regime in Yugoslavia is a legal framework which fails to provide an adequate basis for holding public officials accountable for the exercise of their official functions. Not only does Serbian criminal law not mention the word "corruption" but legislation and regulations written during the 1990s are typically drafted with so much

latitude that they do not support a clear definition of wrong-doing and leave officials ample room to act corruptly within their legally allowed discretion. Laws and regulations typically do not provide public officials with clear parameters within which their decisions are to be taken, instead leaving important decisions to the discretion of individual post holders. A salient example, specific to procurement, is provided by the RS Roads Regulations which, while they specify the basis of operation for Tender Committees, marginalize such committees at the critical juncture of deciding on the award of contract by specifying that "The Committee will submit a protocol on competitive tendering with the documents and report to the Director of the Directorate [of Roads]. The Director of the Directorate proposes the decision on awarding the contract." One of the encouraging aspects of the new procurement laws recently enacted or under preparation in Yugoslavia is that they attempt to rectify this shortcoming.

The RM Procurement Law establishes a more comprehensive framework for accountability, which requires public servants involved in the conduct of procurement, including members of tender committees, to file declarations of their assets with the State Prosecutor. A fresh declaration must be filed when the value of assets and liabilities changes by DM 100,000. This law also has extensive anti-corruption provisions addressing collusion, restriction of competition, bid rigging, kickbacks and a duty to inform State Prosecutor of any breach of these provisions.

A gap in the legislation at all levels is that procurement-related fraud and corruption is not defined as a criminal offence in the criminal law. At the time of discussion of the draft CPAR with the Public Procurement Commission of Montenegro in June 2002, the Montenegrin Ministry of Justice had promulgated an amendment to the Criminal Code of Montenegro which would introduce a new offence of procurement-related fraud and corruption, which would be punishable by a sentence of 1-10 years, depending on the nature of the offence. This amendment is to be encouraged and should be mirrored in the Serbian legislation.

C.3.3 Organization of Public Procurement within Government

The organization of the public procurement function in Yugoslavia is mainly decentralized but with partial centralization of selected procurement functions at the level of both the Republic of Serbia and the Republic of Montenegro.

At the federal level, procurement is fully decentralized to each ministry because each federal institution is autonomous and is the subject of its own Act. There is a federal Mutual Services Agency (MSA), which performs some procurement of common items on behalf of different federal institutions. No single institution performs monitoring or oversight functions for procurement.

In the Republic of Serbia, there is a mixed system of responsibility, with most procurement undertaken by line ministries but some classes of purchases handled centrally by the Serbian MSA, which is deputed under the Budget Act to handle the procurement of cars, computers, maintenance services and electronic data processing (EDP) services on behalf of the Government headquarters, Ministries of the Republic administration and the National Assembly. Other ministries conduct their own procurement and many routinely bypass the MSA, handling themselves the procurement of even those categories of purchases which are intended to be purchased through the MSA.

In the Republic of Montenegro, the new RM Procurement Law establishes an autonomous Department of Procurement Services (DPS), a successor organization to its own Mutual Services Agency, which is responsible for the procurement of commonly used items required by ministries

and departments, where standardization is important – for example, information technology - or where consolidation of requirements is expected to yield more economic results. Procuring entities may choose whether they use the DPS or undertake their own procurement. As yet, neither the list of common items nor the level of charges which DPS may charge for its services has been defined. Therefore, it is too early to tell how well this partially-centralized approach is working. This may also be contributing to the modest volume of procurement so far handled by the DPS: €400,000. In addition, most procurement of civil works contracts for public procuring entities in Montenegro is undertaken by the Department of Public Works.

The majority of procurement, however, is undertaken on a decentralized basis by individual procuring entities. The RM Procurement Law provides for each procuring entity to nominate a number of Public Procurement Officers who take the lead in procurement activities; by April 2002, 123 Public Procurement Officers had been appointed, encompassing the majority of procuring entities governed by the law. While the law authorizes these officers to handle procurement transactions undertaken by the Shopping and Direct Agreement methods themselves, all other procurement methods are handled by Evaluation Committees, the rules of operation for which are defined in the law itself.

C.3.4 Regulatory and Oversight Functions

At the federal level, no institution performs monitoring or oversight functions for public procurement, nor is it currently envisaged that any such regulatory body will be established or deputed.

In the Republic of Serbia, currently no regulatory functions are being performed. However, the draft RS Procurement Act proposes the establishment of a new Public Procurement Office (PPO) reporting directly to the Government. The proposed functions of this new agency, as defined in the law, are listed in Annex D. The PPO is not due to start functioning until one year after the date of effectiveness of the new Act, which likely to be in mid-2003. Until that time, its functions are to be discharged by the RS Mutual Services Agency. It is clear that the successful development of Serbia's public procurement system depends centrally on the establishment and successful operation of this new agency.

In the Republic of Montenegro, by contrast, the RM Procurement Law established a new Public Procurement Commission (PPC), which started operations in September, 2001. The PPC which is, not surprisingly, still finding its feet as an organization, is headed by a President, a retired Supreme Court judge, and staffed by one other lawyer. The PPC needs to be strengthened, both by the addition of more staff and also by the acquisition of office and communications equipment to enable it to function effectively. To its credit, the PPC has launched an Internet website entitled "Public Procurement in the Republic of Montenegro" (www.nabavka.cg.yu), which has quite extensive content in local language, including copies of current legislation and invitations to bid. As yet, however, the English language content of the website is relatively limited, mainly because of the resource constraints on the PPC to add content in a foreign language.

The PPC has performed random checks on about thirty percent of the procurement proceedings conducted by procuring institutions governed by the Law in the period since its establishment and is currently preparing its annual report to Parliament on the functioning of the new public procurement system. It has also visited 10 out of 21 municipalities and has concluded that most of them are applying the new law.

C.3.5 Training of Public Officials in Procurement

At the federal level and in Serbia, very little training in procurement has been provided to the many public officials. As part of its portfolio management function in the country, EBRD has conducted three procurement workshops for public sector clients in Serbia in 2001-2002. The World Bank is planning to conduct procurement training in Yugoslavia in FY03.

In Montenegro, a substantial procurement training program, designed with the assistance of USAID-financed consultants and delivered by the Law Faculty of the University of Montenegro, has so far delivered 7 procurement courses, reaching 308 procurement officers mainly from the central government ministries. The PPC estimates that a further 200 local government procurement officials await initial training. After that, there is an ongoing need to build a training program which can meet the training needs of the public sector on a continuous basis.

C.4 Control Environment

This section reviews internal and external auditing arrangements in FRY, revisits past surveys of procurement-related corruption and examines current anti-corruption programs.

C.4.1 Budget Planning and Execution

The weaknesses in the control environment for public procurement at the **Federation** level and in **Serbia** begin with their respective budget laws, which fail to list the organizations governed by those laws, thus making it difficult to hold public organizations accountable for the expenditure of budget funds, including that on procurement. Lack of compliance with the budget laws further undermines accountability. For example, few ministries submit an annual spending plan to the Mutual Services Agencies (MSAs), despite a requirement to do so.

In addition, while spending entities are required to report back on individual items of expenditure, in practice this does not always occur and, as a result, the Serbian MOFE and Federal MOF have no effective means of monitoring expenditure across different government agencies. The Government's limited ability to control unplanned expenditures and to align commitments with available resources has the effect of increasing unplanned financial outlays, including those on procurement.

Furthermore, the expenditure management system fails to control for past commitments because it focuses on cash controls, —the first stage of the spending process—as they come due. Any unexpected commitment falling due or any shortfall in expected revenues is translated into the creation of arrears or the need to restrict cash releases, which lead to undue disruption and deterioration in government services, including stoppages to payments under existing procurement contracts.

In the **Republic of Montenegro,** both revenues and expenditures are unpredictable for most spending units: government ministries, social funds, public agencies and municipal administrations do not know whether, in any given fiscal year, they will actually receive the funds allocated to them in the annual budget. This is a particular problem for municipalities, which depend on income transferred from the central government for more than half of their revenues. Much of their revenue is collected centrally and fluctuates widely. As a result, there is no multi-year financial planning at the municipal level and almost no capital investment in municipal infrastructure. However, budget execution in Montenegro should improve significantly when the new Budget Law and the new Treasury system are fully implemented.

C.4.2 Current Audit Measures

Internal Controls: The quality of internal financial control and financial reporting is generally very poor in the Republic of Serbia. Elements of financial control have been carried out by internal controllers within some line ministries, the Mutual Services Agency (MSA) and the MOF. However, these controls are limited to basic documentary checks of the accounting and reporting of spending units. They are not conducted systematically nor as part of any overall managerial control to prevent abuse within an organization; rather, they focus on investigations to uncover abuses by public officials in the use of public property and resources. Further

weaknesses within the control system are that there is little or no follow-up to ensure that funds have been spent for the purposes intended and widespread failure to maintain accurate asset registers, which increases the risk of misappropriation of goods procured with public money. The weakness of current asset registration and management practices in Yugoslavia is evidenced by a recent survey which found that seventy percent of prescription drugs procured by the public sector had not reached their intended target.

Scattered and incomplete accounting records, including supporting documentation for purchase transactions, and an inadequate audit trail, further weaken control.

Planned Reform of Internal Controls: The RS MOFE has established a small unit to take forward the introduction of an internal audit function in Serbia, but has yet to define a strategy for the implementation of the internal control environment that is needed to accompany the introduction of the new Budget Law. In Montenegro, many changes to the system of internal control and audit should begin soon, since the new Budget Law, passed on August 9, 2001, is being applied to budget year 2002. The Budget Law is supported by detailed Treasury Regulations that set out much of the groundwork for improved financial control.

Internal Audit: There is currently no Internal Audit (IA) function in the Western sense operating in FRY. The closest parallel is the work done by the Budget Inspectorates (BIs), which carry out compliance work only to check whether internal control procedures are properly followed. The Serbian BI is internal to the executive branch of government but external to individual budget institutions. The Federal Budget Inspectorate is not independent, as it reports to the Federal Minister of Finance and has never carried out inspections of the Federal MOF.

External Audit: There is currently no Supreme Audit Institution (SAI) in FRY, at either the federal or republic levels, with responsibility for carrying out independent, external, ex-post audit in the public sector. No independent external audit has been carried out on Government accounts and final budget accounts have never been audited by independent auditors. The absence of an SAI, reporting independently to the Parliament or operating as part of the judicial process, clearly reduces the counter-balancing effect of the legislature or judiciary over the executive.

In **Serbia**, the new draft Organic Budget Law (OBL) includes a requirement that an external audit report on the financial statements be provided annually to the National Assembly and some limited initial work has been undertaken towards the establishment of an SAI and making it operational by 2003. This will be an essential component of improved public accountability and financial transparency in Serbia.

Montenegro also lacks an SAI with responsibility for carrying out independent, external, ex-post audit in the public sector. Montenegro's government took the initiative of having its 2000 final budget report audited by a private audit firm. However, no progress has been made to date towards setting up an SAI, due to limited knowledge within the public sector of audit issues and limited human and technical capacity to undertake the development of an SAI.

At the **Federal** level, there are currently no plans to develop an external audit body.

It is evident, therefore, that, at all levels of public administration, the institutional architecture for both internal and external control over expenditure has yet to be put in place in Yugoslavia. Its absence no doubt greatly facilitates the presence and growth of corruption and abuses related to procurement.

C.4.3 Corruption

The Legacy of the Milosevic Regime: Administrative decision making in Yugoslavia during the past decade has been overrun by corruption, which was caused by over-regulation of economic activity and excessive discretion given to public officials. Corruption particularly affected trade, business, the public utilities and public services. Among the most common activities which attracted corruption were the systems of licenses, permits and inspections. Many municipalities set informal prices for issuing various types of permits, including building permits. Inspectors in areas such as construction, sanitation, water, health and safety and telecoms routinely demanded bribes for issuing the permits necessary for economic activity to continue. International trade was another magnet for corruption. Smuggling and the obtaining of false certificates of origins were encouraged as means of evading sanctions and the misclassification of goods was widely practiced as a way to reduce tariffs. Government institutions responsible for foreign trade turned a blind eye to these and many other trade-related malpractices. Some municipalities allegedly demanded kickbacks for awarding concessions to operate out-sourced public transport services.[11]

One authoritative study recently described corruption which "permeated every aspect of societal life in Serbia. It was equally present in the judiciary, the police, the health service and public administration."[12]

Procurement-related Corruption: The *Corruption in Serbia*[13] report, published by the Belgrade-based Center for Liberal-Democratic Studies (CLDS), describes a regime in which "public procurement was always done by direct dealing" and "a state in which all significant decisions and transactions were hidden from the public; in these activities, participation was reserved for those picked by the state. They gave offers and were granted deals but had to pay bribes for such contracts." The report describes a system of "informal auction" of government contracts, in which various interest groups would compete, with the winner being "the one who offered the largest bribe."

Other sources paint a similar picture. A representative of Kruševac municipality, addressing a "Workshop on Public Procurement Practice in Serbia" organized jointly by TI Serbia and the United Nations Development Program (UNDP) in April, 2001, described how:

> "in the Socialist era, all public procurement was through only two companies – one was a member of the Socialist party, the other was a house-painting firm. Under the new regime, the old practice of organizing internal tenders continued, so that purchases from the municipal budget are now all made through a football club."

The survey on which the CLDS report was based, conducted in January 2001, demonstrated that the Serbian public perceives corruption in public procurement to be "exceptionally intensive" and that corruption is "an unavoidable side effect of public (state) procurement." Table 3 below, reproduced from the report, presents public perceptions of procurement-related corruption across

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[11] *Breaking with the Past: The Path to Stability and Growth*, The World Bank and European Commission
[12] A GRECO Paper: *Corruption and Anti-Corruption Policy in Serbia*, May, 2001. GRECO is an inter-governmental agreement, under the Council of Europe, for monitoring observance of anti-corruption principles and implementation of the international legal instruments related to its Program of Action against Corruption.
[13] *Corruption in Serbia*, Center for Liberal-Democratic Studies, Belgrade, available at http://www.cipe.org/pdf/Corruption.pdf

seven areas of government operations. With an average perception rating of 4.11 (on a scale of 1 to 5, with 5 being most corrupt), the report describes the health sector as the "epicenter" of procurement-related corruption, though the data suggest that public works may be more severely affected.

Table 3: Assessment of the Spread of Corruption in Public Procurement in Serbia

Field	Average [(a)]	Very	Somewhat	Medium	Some	None	Don't know
Health care	4.11	35	36	15	3	1	9
Education	3.26	10	27	32	18	2	11
Public companies	3.81	21	33	28	4	0.5	13
State administration	3.86	25	30	26	4	1	13
Police	4.04	34	33	13	7	1	2
Army	3.20	14	23	19	2	17	15
Public works	4.16	38	24	12	5	1	19

[(a)] 1 = least corrupt; 5 = most corrupt.

The report characterized corruption in Serbia as a "crisis of morality" responsible for a lack of fairness in society, increasing poverty, the absence of the rule of law, the inefficiency of the judiciary, bad legislation, and the low salaries paid to state employees. It was also found that the absence of a clear condemnation of corruption by government had, in the past, contributed to the public's tolerance of corruption. These findings suggest that any comprehensive attempt to tackle corruption related to public procurement should address all of the identified causes and that the government at all levels must make sure that procurement-related corruption will not be tolerated. Happily, the new Serbian Government has already made clear statements to this effect.

Commonly-observed Abuses in Public Procurement: Both published sources and interviews conducted for this assessment reveal that Yugoslavia suffers from procurement-related abuses which are typical of those observed in other transition countries, including in the other countries which have emerged from SFRY (see the CPAR on Bosnia and Herzegovina). Typical abuses include:

- on separate tenders conducted by the relatively prosperous municipality of Kikinda and the less prosperous municipality of Bosilegrad for similar road rehabilitation works, Kikinda discovered that it had paid more than ten times more than Bosilegrad had paid for the same works. Conferring on the transactions, the two municipalities concluded that local contractors are practicing an abusive form of differential pricing – charging high prices to relatively wealthy municipalities, whom they perceive can afford it.
- on a municipal tender, the same company bid on three tenders under three different names.
- once awarded, many contracts are amended by several "annexes" which increase the total price of the contract several times over.

C.4.4 Current Anti-Corruption Measures

In the Republic of Serbia, since the new Government was formed in January 2001, it has demonstrated commendable vigor in tackling corruption and in breaking any perceived link to the much-publicized abuses of the former regime. Serbia, as with Montenegro, participates in the Stability Pact Anti-Corruption Initiative (SPAI).

Clear political leadership for anti-corruption initiatives has been shown by the Serbian Prime Minister, who has declared his intention that "Corruption should become a highly risky job."[14] The Serbian Minister of Finance and Economy has also overtly recognized that public procurement has been a magnet for corruption, declaring that "It will no longer be possible for, say, health care center directors to have drugs or medical equipment procurement through an inside agreement. Public tenders will be obligatory for all."[15]

The Serbian Government's Strategy for Fighting Corruption[16], launched in December 2001, is built on the following five principles:

- creating an institutional framework: an independent and effective judiciary, stricter legislative branch oversight, an independent, effective public prosecutor and internal affairs organs;
- reform of state administration: establishing standards of professionalism and credibility among public servants, improving the resources available to state administration employees, strict oversight of public revenues, **regulation of public procurement** and monitored decentralization in the fields of public revenues and expenditures;
- economic reform: market liberalization, macroeconomic stability, reduction of discretionary rights in the supervision of economic activity and anti-monopoly policies;
- increased participation by civil society: increased public awareness of the need to fight corruption, facilitating freedom of information, creating forums for public discussion of draft laws and promoting of the role of media and non-governmental organizations in the fight against corruption;
- establishment of an enabling political environment: transparency in the financing of political parties, transparency in the property ownership of state officials and prohibition of conflict of interests between state administration officials and employees.

Among the first fruits of this initiative is a coordinated package of five draft laws, which the Serbian Government prepared during the autumn of 2001, comprising a Law on the Final Account of the Budget for the Year 2000 and Report of the Budgetary Audit; a Law on the Budgetary System; a **Law on Public Procurement**; a Law on Games of Chance, and a Law on Tobacco.

Among the institutional arrangements which have been put in place to deliver this strategy are:

- an independent **Anti-Corruption Council** was established in December 2001 and has been charged with the development of National Anti-Corruption Strategy. The ACC advises the Government on legal reform and development and conducts studies of corruption in society. In the first two months of its operation, the Council advised the Government the drafting of several laws, including the Law on the Prevention of Conflicts of Interest, the Law on Financing of Political Parties and the Law on Property of State Officials. The Council also acts as a watchdog, monitoring actual cases of corruption and calling the Government to account for any perceived slippages in its anti-corruption program. Transparency International Serbia is a prominent member of the ACC.

[14] "Government forms regional network of anti-corruption team," Office of Communication of the Serbian Government, January 19, 2002.
[15] "Serbia has the institutions to fight corruption," January 24, 2002 available at www.serbia.sr.gov.yu/news/2002-01/24/322228.html
[16] The Serbian Government's Strategy for Fighting Corruption, available at www.serbia.sr.gov.yu/transition/fighting_corruption

- a **High-Level Anti-Corruption Committee**, headed by the Prime Minister and comprising several key Ministers and heads of key public agencies, whose role is to steer the implementation of the Government's anti-corruption program.
- an **Anti-Corruption Unit** which was set up to act as the headquarters of the anti-corruption initiative in Serbia is strategically located within MOFE. The office coordinates all anti-corruption initiatives, ensures information exchange between the parties involved and assists both Government and NGO anti-corruption initiatives.
- a **Regional Network of 26 Anti-Corruption Teams**, set up in January 2002, whose job is to protect citizens' rights from misuse by state officials of their position. In the period January 15-April 25, 2002, these teams received 1,113 calls from members of the public reporting allegations of corrupt conduct by public officials, 78 of whom decided to file written criminal charges in person. The majority of the calls were registered in Belgrade, Novi Sad, Nis and Vranje.

To its credit, the new Government has shown welcome signs of a new openness, regularly updating its achievements against its anti-corruption program on its website (see footnote 7 below) and publishing targets for outstanding actions. In addition to the preparation of the new Law on Public Procurement, a recent related achievement is a prohibition against Serbian Government members engaging in business activities.

Key institutions of the Serbian Government involved in the fight against corruption, including the Ministry of Internal Affairs and the Belgrade District Attorney's Office, also publish reports of their activities on the government website, including the names of former state officials and employees charged with abuses of power or of making material gain from public office. The Ministry of Internal Affairs reports having brought criminal charges against 209 members of its own staff during the period January – October 2001.

In the Republic of Montenegro, the Government has also made significant efforts to combat corruption. In February 2000, Montenegro accepted the Stability Pact Anti-Corruption Initiative (SPAI) Compact and Action Plan. It has also established a separate government agency, the Anti-Corruption Initiative Agency, which has responsibility for preparing draft laws and sub-legal regulations; adopting international documents and standards and monitoring their implementation; defining an anti-corruption strategy; promoting transparency and integrity in business transactions and monitoring the privatization process; undertaking public awareness and prevention activities; and coordinating the activities of both governmental and non-governmental sectors aimed at curbing corruption.

In 2001, two important pieces of legislation containing anti-corruption provisions were passed: the Public Procurement Act and the Organic Budget Law. The Government is also working on a draft Code of Conduct for Civil Servants, a Conflict of Interest Law, Freedom of Information Act, an Illicit Enrichment Law, an Anti-Money Laundering Law and a Law on the Financing of Political Parties.

The Government has also made strides in involving civil society in its anti-corruption drive, establishing, jointly with the NGO sector, a cross-cutting Committee for Anti-Corruption to review the National Strategy for Anti-Corruption and to work on the preparation of new legislation.

At the Federation level, the Federal Government has yet to develop a coherent anti-corruption program and has not embraced the anti-corruption challenge as eagerly as the governments of the two republics.

C.5 Public-Sector Management Performance

This section attempts to quantify, based on currently available budget data, the value of expenditures on public procurement by the various levels of administration in FRY and examines the extent to which value for money is achieved by current procurement practices in the health sector.

Given that neither the Federal MOF, nor the RS MOFE nor the RM MOF collects or publishes any information on expenditures on public procurement, an attempt at quantifying these expenditures for this assessment has relied on budget data published by the International Monetary Fund (IMF), as well on data collected by the World Bank in the course of the PEIR.

Public procurement makes up a substantial component of total budgeted expenditures in FRY, representing some 24 percent of total public expenditure in 2001 or about 10.15 percent of GDP (see Table 4 below). This figure is close to the levels of expenditure on procurement observed in more economically developed countries. For example, in the European Union, public procurement accounts for 11-12 percent of GDP. The high rate of inflation, which averaged 91.1 percent in 2001, has substantially eroded the value of that investment in real terms, despite increasing capital expenditure, mainly in infrastructure, during 2001 and 2002. In Montenegro, public procurement has been steadily declining year-on-year as the Government's budget shortfalls have forced cut-backs in both recurrent expenditures and capital investments in infrastructure.

Table 4: Expenditures on Public Procurement by the FRY (Serbia/Montenegro) 2000-2002 (includes social funds)

	2000		2001		2002*	
	USD (M)	% of GDP	USD (M)	% of GDP	USD (M)	% of GDP
1. Total Expenditure	3,266.44	36.19%	4,638.63	42.71%	6,256.06	48.72%
of which:						
a. Goods and Services	688.75	7.87%	953.51	11.81%	1,053.82	8.21%
b. Capital Expenditure	268.27	3.07%	149.25	1.85%	398.98	3.11%
2. Total Procurement Expenditure (1a+1b)	957.02		1,102.76		1,452.80	
As a % of Total Expenditure	29.30%		23.77%		23.22%	
As a % of GDP	11.86%		10.15%		11.31%	
GDP	8,071.00		10,861.00		12,841.00	
YuD Avg Inflation (Retail Price)	69.90%		91.10%		26.30%	

**Budget*

At the federal level, of the 2001 budget of YuD 45.8 billion, 70 percent was allocated to Defense and the remaining 30 percent to the civil administration. The Federal Ministry of Finance estimates two-thirds of total defense expenditure is spent on non-military requirements, for example, on passenger vehicles, uniforms and foodstuffs. While it is normal practice in most countries that military procurement is legislated separately from civil procurement, it is equally common practice that non-military spending by the defense forces comes within the compass of the civil procurement law. It should, therefore, be an objective of the Federal Government to make non-military procurement undertaken by the defense forces subject to the application of civil public procurement law, when enacted.

Currently, each of the ten federal ministries undertakes its own procurement and none of it is subjected to tendering.

Background to Pharmaceuticals Procurement in Serbia

Eighteen percent of total health sector expenditure in Serbia is spent on pharmaceuticals, a figure which is in line with Western European countries, where the range is 15-20 percent. Yet, for some years now, Serbia has been chronically short of drugs.

Public procurement of pharmaceuticals in Serbia has historically taken place in a highly controlled marketplace, typified by excessive closeness between the main public consumer, the Ministry of Health of the Republic of Serbia, and a small number of domestic manufacturers, represented by a fifteen company-strong cartel, the Industry Lobby of Pharmaceuticals Manufacturers. Until recently, it was MOH's regular practice to enter into negotiations every two months with the lobby group, at which they defined the list of pharmaceutical products to be supplied, the quantities required and the prices to be paid for about seventy percent of public demand (the remaining 30 percent comes from other former SFRY republics, primarily Slovenia, with only 5 percent from Western Europe). Within these parameters, the lobby group would decide how the supply of drugs and quantities would be divided up among with fifteen members and, where two or more manufacturers supplied the same drug, they could each be paid the same price. In all respects, therefore, public-sector procurement of pharmaceuticals has, until recently, taken place in a near-closed market, characterized by untransparent negotiation and devoid of any meaningful competition.

A further barrier to competition, especially to foreign manufacturers, is posed by drug registration, the procedures for which are both bureaucratic and extremely lengthy. Of the 722 drugs currently registered, only 133 (18.4%) are registered by 3 or more producers/suppliers, which clearly limits the Government's ability to generate competition to supply those items to meet public demand.

The market has also suffered from other dysfunctions. Primary among them has been an absence of efficient planning, so that the quantities of drugs requisitioned by the MOH are not based on any formal quantification of the real needs of the public or of healthcare institutions. This disconnect has been one of the main contributing factors to the chronic shortages of urgently needed drugs. In addition, the list of approved drugs, whose cost the RS Health Insurance Fund (HIF) is obliged to meet, has in the past been excessively long at some 400 drugs (the Essential Drugs List of the World Health Organization is 150 items), placing an unsustainable burden on the HIF, although the Government has recently taken steps to reduce the size of the list to 321. The maximum wholesale prices for approved domestically-produced drugs are set by the Federal Ministry of Economy and Internal Trade and are calculated on the basis of forty-seven percent of prices for the same drugs in Slovenia, though the paucity of Government information systems is such that often the Government does not have up-to-date information on drug prices in that country.

Demands on the limited resources of the HIF are heightened by the repeated failure of the public healthcare system to make available through public pharmacies, approved drugs which patients have a right to obtain under prescription. In all cases where a public pharmacy fails to fulfill such a prescription, the patient has the right to obtain the prescribed drug from a private pharmacy and to obtain a refund of the additional cost from the HIF. The European Agency for Reconstruction (EAR) estimates that, in 2001, such reimbursements were costing the HIF some YuD 15.0 million (US$227,000) each month, an avoidable cost which the HIF call ill-afford to meet.

These difficult circumstances have been further exacerbated by a lack of clarity in the respective roles and responsibilities of the RS Ministry of Health and the Health Insurance Fund, although a re-definition of this relationship is being addressed by a new Law on Health Insurance, on which the Government has recently been working. One symptom of this lack of clarity is that there have been several instances where public hospitals have proceeded to undertake procurement of pharmaceuticals to meet their own needs, without consulting the HIF, and have subsequently billed the HIF for the cost of these drugs. The HIF is obliged to meet these costs, without having been consulted on the specifications, quantities or prices paid. This situation has been exacerbated by a severe problem of publicly-procured drugs "leaking" into the black market and finding their way into private pharmacies, due to poor inventory control in the public pharmacies.

Weak coordination of requirements with external agencies financing the procurement of drugs in Serbia has caused further confusion. This has led to instances of over-supply of certain items, which have been procured by both the Government of Serbia and an external institution, whilst shortages of other approved drugs continue.

Two Surveys of Pharmaceuticals Prices in Serbia

While a nation-wide survey of the cost-effectiveness of public procurement in Yugoslavia was beyond the scope of this assignment, the mission undertook a limited analysis of historical prices paid for selected pharmaceuticals and medical consumables from a series of procurement transactions in Serbia during 2001. The objective of this exercise was to compare federally mandated prices, prices actually paid under local tenders financed by the Serbian HIF and prices for the same products resulting from competitive tenders financed by external sources (Pharmaciens Sans Frontières and the European Agency for Reconstruction), so as to form an opinion as to whether prices paid for commonly-procured pharmaceuticals and materials offer reasonable value for money.

To achieve this, the assessment looked at price data from four tenders. In the first (see Annex E.1), prices paid for 21 locally-manufactured cardiovascular, respiratory and diabetes drugs as well as some medical supplies, as a result of two local tenders financed by the EAR in September and December 2001, were compared with the prices published by the Federal Ministry of Economy and Internal Trade for the same items. The latter prices are those which the RS Health Insurance Fund is authorized to finance. For the 21 products purchased, the EAR-financed price was lower for 17 products and higher in the other 4 cases. In the 4 cases where the EAR-financed price was higher than the federally sanctioned price, the difference in price ranged from 4.29% to 18.36%. In the 17 cases where the EAR-financed price was lower than the federally approved price, the difference ranged from 4.89% lower to 175% lower for one item. Taking the average of the 21 products purchased, the prices paid under the EAR-financed tender were 36.2% lower than federally approved prices. Finally, the total quantities of all 21 pharmaceutical products procured by the EAR cost a total of €4,085,353 (US$3,728,784 equivalent); had these products been procured in the same quantities at federally approved prices, the total cost would have been €5,493,574 (US$5,014,096),. This translates into a notional saving of €1,408,221 (US$1,285,311) or 25.6%.

Separately, the assessment analyzed prices paid for 46 drugs from a wider range (cardiovascular, respiratory, antineoplastics, antidiabetics, pain killers, anti-infectives) as a result of local purchase transactions made by the Serbian Health Insurance Fund in April 2001 and compared them with prices paid following a local tender operated by PSF in March 2001 for three months' supply of the same drugs. Having calculated the cost of the estimated annual supply of these 46 drugs, the

costs incurred by the HIF were calculated to be 23.7% higher in total than those based on the prices paid by PSF for a year's supply of those drugs (see Annex E.2).

The findings of these surveys are consistent with other, more wide-ranging surveys of the effects of the introduction of competitive tendering on prices paid in public procurement. For example, one well-known survey found that competitive contracting by the public sector in the United Kingdom yielded savings in the order of 20% without any reduction in quality.[17]

[17] 'Contracting Out by the Public Sector: Theory, Evidence, Prospects" Domberger and Jensen, Oxford Review of Economic Policy, Vol. 13, No. 4, 1997.

C.6 Performance on Projects Financed by the World Bank and EBRD

This section reviews the experience to date of the Government's performance to date of procurement in accordance with the World Bank's procurement guidelines on Bank-financed projects and highlights problems affecting procurement performance and suggests a series of measures to be taken to tighten fiduciary control of future procurement operations to be financed by the World Bank in FRY.

With Yugoslavia having rejoined the World Bank so recently, there is little experience to go on when assessing the ability of public sector procuring entities to implement public procurement in accordance with the two institutions' procurement guidelines.

However, while little of the expertise built up during Yugoslavia's earlier membership of the World Bank remains, the performance of most procuring entities has been surprisingly good, albeit supported in most cases by external consulting services. Staff in procuring entities handling procurement are generally well-educated, have good foreign language skills and sound technical knowledge. Also, the timeliness of procurement is generally good and staff in the implementing agencies display an impressive commitment to follow the Bank's procurement guidelines diligently.

The experience on public-sector projects financed by EBRD is similarly encouraging.

C.6.1 Measures to Strengthen Fiduciary Safeguard on World Bank-financed Projects

In order to reduce any risk to World Bank funds disbursed on procurement under Bank-financed projects in Yugoslavia, the Bank should take the following steps:

- At appraisal of all new projects, undertake an assessment of the institutional capacity of all agencies involved in the project to implement procurement under Bank guidelines. Where capacity is found to be weak, put in place a detailed action plan to supplement and/or develop capacity to undertake procurement satisfactorily;
- Prepare a detailed procurement plan should be prepared that is approved by the Bank at appraisal. Bank staff are expected to follow up assiduously to make sure that plans are kept up-to-date and where slippage does occur, that remedial action is taken promptly by both the Borrower and the Bank.
- Bank Task Team Leaders and procurement staff should make sure that the procurement staff of implementing agencies are appointed following a competitive process and that they are fully qualified.
- Keep thresholds for prior review relatively low, e.g. >US$100,000 for goods, so that most contracts fall above the prior review threshold and are subject to prior review by the Bank.
- Although no procurement post reviews have been conducted to date, Bank task teams should ensure that the level of post reviews conducted is kept at the level stipulated in the various loan/credit agreements.
- Procurement by less competitive procurement methods, including International Shopping and National Shopping, should be kept to a minimum for all new projects.
- The Regional Procurement Adviser (RPA), the Bank's most senior procurement official for Europe and Central Asia (ECA) Region, should assiduously follow up any procurement-related complaints submitted by bidders.
- Where allegations of procurement-related fraud or corruption are received, the Bank's Investigations Unit should investigate them assiduously.

C.7 Risk Assessment

Any assessment of risk in a country's national public procurement system should be based on the stage of development of its legislative framework, the effectiveness of its regulatory institutions, the strength of its enforcement regime, the capacity of its institutional and human resources and the threat of corruption.

- FRY's **legal framework** is both incomplete and insufficiently robust to provide for a clear, rules-based environment for conducting public procurement. At the federal level, no specific law governs procurement, existing sub-legislative provisions are wholly inadequate and there is no regulatory function in place. In Serbia, current regulations offer only partial coverage in selected sectors, their provisions fall far short of a comprehensive framework and excessive discretion of placed in the hands of senior decision-makers without proper accountability. A new draft RS Procurement Law is under preparation but it has a number of provisions which fail the test of real transparency. In Montenegro, a good new law has recently been placed on the statute book, but its effectiveness in implementation is only just being tested and is as yet unsupported by the necessary implementing regulations, which will be required to clarify its application.
- **Regulatory functions** for public procurement are a particular weakness of the Yugoslav system. At both federal and Serbian levels, no regulatory body has been established. While the new draft RS Procurement Act provides for the establishment of an independent Public Procurement Office, it will not be in place for a year or more and the agency which is to perform its functions for the first year after enactment of the Act, the Mutual Services Agency, lacks the institutional resources to carry out these tasks effectively. In Montenegro, a new Public Procurement Commission has been established, but it is under-staffed and lacks both the physical and systems resources to do its job to full effect.
- The **enforcement regime** which underpins the procurement legislation is also weak. Both internal and external auditing are absent and current mechanisms for reviewing bidders' complaints are either completely absent (Federation, Serbia) or unproven (Montenegro). As a result, public officials are not being held accountable for the decisions they make about procurement.
- With a few exceptions, the **public sector institutions** which conduct procurement are ill-equipped for the task. Most ministries do not have dedicated organizational units to undertake procurement, and **staff** who handle the task invariably do so without training. The entire country lacks a planned training system for procurement.
- **Corruption** is widely recognized as being a widespread and serious problem and appends itself particularly to public procurement, given the substantial expenditure which all levels of administration make in this area. Whilst anti-corruption efforts are under way, they cannot be expected to solve the problem of procurement-related corruption in the short term.

Measured against all of these parameters, the environment for conducting public procurement in Yugoslavia is characterized by a high level of risk.

C.8 Recommended Supervision Plan

The following financial thresholds for procurement methods are recommended:

Table 5: Applicable Thresholds by Procurement Method

Procurement Method	Threshold
ICB: Works	>US$100,000
Minor Works	<US$100,000
ICB: Goods	>US$100,000
International Shopping: Goods	<US$100,000
National Shopping: Goods	<US$50,000

Under the procurement guidelines of both the World Bank and the EBRD, National Competitive Bidding (NCB under WB guidelines) or Local Competitive Tendering (LCT under EBRD procurement rules), before NCB/LCT can be permitted, each Bank has to determine whether or not the national procedures are satisfactory. Given the absence of specific procurement laws and the federal and Serbian levels, national procedures cannot be considered satisfactory to either institution at the time of preparation of this report. Therefore, the World Bank will await the passage of the Serbian Law on Public Procurement before agreeing that NCB may be conducted on the projects which it finances there. In Montenegro, a separate side letter, detailing the waivers which will be required from the current procurement law, will be prepared by the Bank when it next finances a project in Montenegro which requires the use of the NCB procurement method. Simultaneously, EBRD will work with its clients to develop an acceptable procedure for the procurement of low value contracts on a project by project basis, until such time as an appropriate national procurement law is enacted.

In the selection of consulting firms, shortlists may comprise entirely national consulting firms if the assignment is estimated to cost less than US$100,000, provided further that there are available a sufficient number of qualified national firms to provide adequate competition at competitive costs.

The Bank should conduct **Prior Review** for every project on:

- all contracts for Goods and Works procured by ICB;
- contracts with consulting firms >US$50,000; and
- contracts with individual consultants >US$25,000.

At least 1 in 5 of contracts which are subject to post review should be post reviewed by the Bank.

Given the relatively under-developed state of Yugoslavia's consulting industry, shortlists for consulting assignments on Bank-financed projects may comprise entirely national consulting firms only if the assignment is estimated to cost less than US$100,000. Bank task teams should make a determination, on a project-by-project basis, that there is a sufficient number of qualified firms to provide adequate competition at competitive cost.

In cases where Bank funds are on-lent through financial intermediaries in accordance with paragraph 3.12 of the Bank's Procurement Guidelines, procurement of contracts for goods and

works estimated to cost less than US$250,000 per contract may be undertaken in accordance with established commercial practices acceptable to the Bank.

C.8.1 Future Conduct of National Competitive Bidding on World Bank-financed Projects

Given that there is currently no procurement law at the federal level and none in the Republic of Serbia, the Bank cannot agree to the conduct of National Competitive Bidding (NCB) because of the absence of acceptable local procedures. However, once the draft RS Procurement Act has been enacted and entered into force, the Bank will review the provisions of that law as enacted and will propose to the Government a side letter, to be appended to future loan agreements, specifying variations to its provisions which may be required for the conduct of NCB on future Bank-financed projects.

In Montenegro, current Bank operations do not include any NCB procedures. Again, if future Bank-financed operations require NCB, the Bank will propose to the Government a side letter defining any necessary variations to the RM Procurement Law.

PRIVATE SECTOR

This section examines the extent to which the private sector is able to supply public-sector demand, describes commercial purchasing practices in the private sector itself, and reflects a view of the country's public procurement system from the perspective of the private-sector companies interviewed for the assessment.

C.9 Competitiveness and Participation of the Private Sector

Unlike many other Eastern European countries, which have suffered from a Communist-era legacy of over-concentration on heavy industry, Yugoslavia's inheritance from the Titoist economic experiment was a diversified industrial base, which included food processing, auto manufacturing, textiles, chemicals, furniture manufacturing, and a construction sector which was both technologically advanced and internationally competitive. However, this promising legacy has been laid to waste by a decade of economic isolation, the loss of key markets in the other Yugoslav republics – exports, mainly comprising manufactured goods, plummeted from US$4.1 billion in 1990 to just US$1.7 billion in 2000 - and the physical damage wrought by the NATO air strikes of March-June 1999, which either damaged or destroyed some 40 major industrial complexes and more than 100 other large businesses.

From the early 1990s onwards, industrial production was already in sharp decline due to the breakup of Yugoslavia. Production fell by 15.9 percent in 1991, the first year of war, and declined again in both 1992 and 1993. After sanctions were suspended in 1995, production experienced modest recoveries of 7.5 percent in 1996 and 9.6 percent in 1997, slowing to growth of 3.4 percent in 1998, before falling sharply by 23.1 percent in 1999. The severity of the challenge which faces the new Government in arresting this alarming industrial decline is further illustrated by the fact that, in the first half of 2001, when the new Government had taken over, industrial output fell again by 2.4 percent. This difficult situation is exacerbated by supply-side problems in the economy, including a chronic lack of investment, the inability of Yugoslav firms to meet international quality standards, and recurring energy shortages, which act as a brake on output. There is an urgent need for fresh investment in the industrial sector which, given the weakness of the country's financial and banking sector, will have to come largely from foreign sources, particularly in the form of Foreign Direct Investment (FDI).

To complicate the picture further, the years of war, with their concomitant weakening in the rule of law and the collapse of legitimate economic activity, have been accompanied by a mushrooming of the "gray economy" in Serbia, which one recent estimate suggests accounts for as much as 50 percent of the Republic's GDP.[18] The gray economy in FRY takes the form of unregistered employment and conduct of business and illegal trafficking of excisable products, particularly oil products, cigarettes and alcoholic beverages. These activities developed during the 1990s, when the combined effect of low salaries, high unemployment, and impediments to normal trade during sanctions created both a need and an opportunity for informal sector activity. The greatest relative importance of the gray economy was at the time of hyperinflation in 1993, when it accounted for more than one-third of economic activity and more than half of registered social product (54 percent).

[18] "Serbian Bureaucracy Threatens Democratic Reform" Center for International Private Enterprise, November 19, 2001.

Privatization

Table 6: Social Product by Form of Ownership, 1999		
	YuD (M)	**%**
Privately-owned	69,361.5	42.4
Socially owned	45,913.0	28.1
Mixed ownership	42,882.2	26.2
State-owned	3,070.7	1.9
Cooperative	2,239.2	1.4
Total Social Product	163,466.6	100.0
Source: Federal Statistics Office		

The privatization process, which began in Yugoslavia in 1989 with the passage of the Federal Law on Privatization, was interrupted by the conflicts of the early- to mid-1990s and further undermined by sanctions, which cut the country off from foreign investment. As late as 1999, private-sector ownership accounted for only 42.4 percent of Social Product (see Table 6), with Yugoslavia's unique form of "socially owned enterprises" still accounting for more than 28 percent of Social Product.

C.9.1 Construction Sector

Yugoslavia's once globally competitive construction industry has been in sharp decline throughout the past decade. Ten years ago, some 50 percent of the construction output was produced abroad, mainly in Yugoslavia's once lucrative overseas markets in the non-aligned countries of Eastern Europe and the Middle East. During the sanctions period, those markets were lost. There are now about 5,000 active companies in the sector, including construction companies, project engineering firms, and materials suppliers. The great majority of these, around 85 percent, are privately owned, with the remainder being either publicly or socially owned. The largest companies employ in excess of 1,000 people and have annual turnovers of up to US$150 million, with average contract values in the range of US$10 to 30 million. There are also many small contractors employing fewer than 50 people. The construction sector, which now accounts for about 6 percent of GDP, has both the capacity and capability to meet present domestic demand. Indeed, the industry is currently operating below capacity and is, therefore, underutilized.

The decline of the sector can be traced in annual changes in construction activity, measured by the number of hours worked annually. This measure continued to decline even after the lifting of sanctions in 1995, although at a slower pace than in previous years; the decline accelerated in 1999, as a result of the Kosovo crisis and sanctions (see Table 7).

Table 7: Construction Industry Activity in Yugoslavia, 1996-1999

	1996	**1997**	**1998**	**1999**
Hours of work completed (millions)	99	96	90	69
% change year on year	-9	-3	-6	-22

Source: Federal Statistics Office

The legacy of these troubled years is a construction industry which has been starved of business opportunities and investment. Many construction contractors are struggling with inadequate capacity, a shortage of workers skilled in new technologies, outdated management skills– (for example, in areas such as scheduling, quality control and contract management) and obsolete equipment. Most contractors have been unable to afford the purchase of new plant and capital equipment during the past decade. In a recent survey of barriers to investment in Montenegro,

over half of construction firms cited obsolete or insufficient capacity as a major hindrance to the development of their business.[19]

A further constraint on the regeneration of the sector has been posed by unreliable availability and poor quality of construction materials, due to a combination of lack of investment, high taxes, import restrictions, price distortions, and a lack of research and development. These factors have contributed to a situation in which locally available construction materials are generally technologically less advanced and efficient than in other countries. Until recently, the government would allow only a few companies to import construction materials and equipment under license, which enabled these companies to influence and distort market prices. There are signs that this practice is changing and prices are becoming more liberalized. Nevertheless, prices of imported construction materials in Yugoslavia are still above international market prices.

C.9.2 Banking Sector

Yugoslavia's banking sector is deeply insolvent as a result of structural problems inherited from the pre-1991 socialist system and a decade of mismanagement that followed the breakup of SFRY. Throughout the last decade, FRY's financial system has operated under extremely harsh conditions of economic instability, high inflation, massive defaults and arrears and economic sanctions. Significant portions of the banks' balance sheets were non-earning assets, either immobile or non-performing. Mismanagement of the large banks took the form of directed credits ordered by the government and was exacerbated by ownership or control exercised over the large banks by some of the large and troubled state- or socially-owned enterprises. The sector shrank significantly during this period: total banking system assets declined by more than one quarter since 1994 to an estimated DEM 23 billion in 2000. Bank deposits are predominantly short-term and lending is limited to retail trade transactions. Deposit interest rates have remained negative in real terms, discouraging domestic savings and resulting in high lending rates. By 1997, savings had slumped to below DEM 100 per capita, starving the banks of much-needed liquidity. While the World Bank's Transitional Support Strategy (TSS) for Yugoslavia recognizes that a well-functioning financial sector is essential for private sector-led growth, the banking sector does not currently enjoy the kind of legal and institutional framework necessary to support the development of a conducive business environment.

All construction firms in Yugoslavia have difficulty in obtaining bank guarantees or securities, partly due to their parlous finances but also because illiquid local banks demand at least 110 percent cash cover to issue such instruments. Some also require that such instruments be secured against real property to a value of two to three times the value of the guarantee. The weakness of Yugoslavia's banking sector also acts as a restraint on Yugoslav firms' efforts to regain their former position in overseas markets, as most potential foreign customers are unwilling to accept bank guarantees issued by Yugoslav banks. The difficulty, which these firms have in accessing affordable long-term credit, is a further serious obstacle to their regeneration.

C.9.3 Private Sector Perspectives on Public Procurement

The majority of bidders interviewed for this assessment do not actively pursue public-sector contract opportunities because they are concerned the time and cost of bidding will be wasted by

[19] "Barriers to Investment in Montenegro" Center for Entrepreneurship and Economic Development, Podgorica, 2000, based on a survey of 469 Montenegrin firms.

untransparent application of the procurement procedures or by arbitrary or corrupt contract awards. Even if they win a public-sector contract, many bidders worry about the poor contract management capability of public authorities, which frequently turn a contract, which is profitable at signature into a loss-making experience for the supplier or contractor. Reported problems include late payments, unjustified suspension of works and arbitrary cancellation of contracts. While some contracts have been cancelled because of the change in Government – the new Government cancelled contracts placed by the previous regime, fearing they were corrupt or delivered poor value for public money – there is a general concern among contractors that contractual relationships with the public sector are not reliable. Most bidders professed to having no idea how public officials make decisions about awarding procurement contracts, as the criteria for evaluating bids are not disclosed to them in advance.

Construction contractors complain of being starved of business opportunities, given the fall-off in capital investments by both public- and private-sector clients. A contractor interviewed for this assessment, one of the five largest in the country, had not seen an invitation to bid from a public client in more than a year. This paucity of opportunity has spawned cutthroat competition between bidders for the few tendering opportunities, which arise; including offering clients deferred payments for periods of as much as the first year of a contract. Given that new construction projects invariably have high start-up costs, such practices look certain to undermine the feasibility of new projects and to reduce the contractor's profit.

C.9.4 Performance on Public Contracts

As has been described above, Yugoslavia's once globally competitive construction industry has been substantially reduced by almost a decade of economic isolation from the world's markets. The effects of this isolation can be seen in the greatly reduced ability of local firms to perform satisfactorily on public contracts. Their performance has been weakened by chronic under-investment, a severe shortage of credit, outdated plant and equipment and management and labor skills, which have fallen behind international standards. These constraints, when combined with the public sector's own budgeting and liquidity problems, mean that delays in the implementation of contracts are relatively common in Yugoslavia.

C.9.5 Commercial Regulations

As has been the case in other former constituent republics of the SFRY, Yugoslavia has embarked upon a comprehensive program of legislative, commercial, and judicial reform. It is estimated that 85 percent of the economic laws are slated for reform or replacement in the next one to two years,[20] including those in the areas of foreign investment and foreign trade, foreign currency transactions, insolvency, taxation, property, privatization, collateral, labor, and legislation in various service sectors including telecommunications, legal profession, insurance, road transport, maritime transport, auditing, and banking.

A common characteristic of various laws in the FRY, including the Foreign Trade Transactions Law, is the presence of formulations that often lead to excessive administrative discretion, restrictive regulation of foreign trade, and unpredictability in the legal environment for commerce and investment. This situation is about to change, however, as the governments of Yugoslavia,

[20] Report on the Status of Commercial Legal and Institutional Reform as the Foundation for Long-Term Strategy Development, United States Agency for International Development, August 2001.

Serbia and Montenegro liberalize, deregulate and harmonize laws with developed market-oriented legal systems. The need for further legislative development in the commercial sphere will no doubt be magnified by the FRY's formal WTO accession process and by the anticipated conclusion of a Partnership and Cooperation Agreement with the EU, as each of those processes will entail alignment and approximation of legislation with applicable international standards.

Having started first and with the assistance of a wide-ranging USAID Technical Assistance program, Montenegro is the more advanced in this reform effort, but the new government in Serbia has also made an energetic start to legislative reform since taking office at the beginning of 2001.

The federal level has probably the further to go but its active participation in these reforms is essential, given the broad jurisdiction which Article 117 of the Federal Constitution bestows upon it. At this point in time, it is difficult to forecast the precise distribution of legislative competencies among the component parts of the prospective new state that would be established as Serbia and Montenegro, but in the FRY as it stands now, the federal government has jurisdiction over the legal status of enterprises and other economic agents (company and insolvency laws); the monetary, banking, and foreign exchange systems; foreign trade regulation and foreign investment, including: contract relations; basic property legal relations; civil procedure laws; protection of the single Yugoslav market (internal trade and competition law); the legal status of companies and other economic operators; customs; credit relationships with foreign countries; the fundamental principles of the fiscal system (monetary and banking law and foreign currency), social security, pricing policy and labor; transportation safety; rights and obligations under contract; property law and basics of the tax system. The republics regulate, in particular, land ownership and zoning, privatization, and sanitary and fire inspection. The federal and republican levels share regulatory authority over matters including: technical standards, licensing, and qualification requirements for the conduct of services; education; environmental protection; social security, taxation and pricing policy

Law on Obligations: One of the main bodies of law pertaining to commercial activity is the Law on Obligations, inspired primarily by the Swiss Code of Obligations. One of the few bodies of legislation to have largely survived the breakup of the SFRY, the Law is widely regarded as one of the best pieces of legislation in the FRY. The law serves as a code setting forth rights and obligations of parties in a wide variety of situations, both contractual and non-contractual, and, as such, serves some of the purposes of the general part of a civil code. The Law provides extensive regulation of general contract law and commercial variations thereto, setting forth the basic principles of, for example: formation of contracts, agency, fundamental principles and effects of contracts, illicit enrichment, liability for causing damage, securities, termination of obligation, general rules of performance, prescription period, various types of obligations, and various types of contracts (e.g., sale, transport, loan, lease, contracts for works (services), construction, and others). An important positive feature of the Law is the recognition of the contractual freedom of parties, which also allows the law to accommodate the introduction of contractual forms not specifically referred to in the law.

The Law on Obligations is held in high regard in the FRY legal community as meeting most of the contract law needs of market economy. However, various additions of detail and some modifications, clarifications and updating would be useful such as modernizing the rules of construction by inclusion of subsequent behavior of the contracting parties, and updating provisions on documentary credits to reflect the latest version of the Uniform Code of Practice (UCP). One drawback of the law is the wide berth given to courts to intervene in and alter the terms of contractual relationships.

Foreign Trade Law: The primary legal instruments for regulating foreign trade include the Law on Foreign Trade Transactions (the FTT Law) and the Customs Tariff Law. Recent amendments to that framework have included: reductions in quantitative restrictions on imports and in import license requirements, though a substantial number of both remain in place; establishment of a new tariff structure; some diminution in administrative barriers including elimination of minimum size for companies in foreign trade; and elimination of annual registration tax applied to trading companies. However, considerable further amendments would be required to establish a legal framework more amenable to foreign trade and fully in line with WTO standards.

The FTT Law, covering trade in goods and some aspects of trade in services, derives from the semi-planned economy context, where foreign trade was the province of socially-owned, politically-controlled enterprises. When applied in the current incipient market-based environment, the FTT Law allows for continued intrusive governmental involvement in the operations of private-sector importers, exporters and service suppliers. Such unwarranted provisions include those purporting to regulate business activities abroad, registration requirements still applied to those conducting foreign trade, quantitative quotas on exports, governmental approval requirements for co-production agreements, authorization to impose public procurement types of procedures on some private sector imports, the apparent application of public bidding procedures to the award of "capital project" works contracts and the required hiring of local contractors; mandatory registration of "capital contracts" to be performed either in FRY or abroad and a requirement that a government authority determine the obligatory contents of capital project contracts. A distinctly preferable, more contemporary approach would be to abolish FTT Law entirely and regulate foreign trade in the new Law on Trade, which is currently being drafted. In Montenegro, import quotas have already been abolished and steps have been taken to simplify import procedures. The import-export regime is now regulated by the Law on Foreign Trade.

Customs: According to Article 77 of the FRY Constitution, the Customs function falls under the jurisdiction of the federal state. However, Montenegro has assumed control over the regulation of Customs and the collection of duties and taxes on its territory. In July 2000, Montenegro adopted a Temporary Act on Customs Tariffs, which introduced lower tariffs than at the Federal level. The Montenegrin Customs Administration (MCA) operates independently de facto, and the Federal Customs Administration (FCA) primarily covers the Serbian territory. While informal cooperation has been maintained between the two administrations, the juxtaposition of two Customs systems creates opportunities and incentives for corruption and smuggling. Although checkpoints have been established at the administrative border between the two republics to address this problem, these checkpoints create an additional bottleneck for internal transit.

Customs operations in FRY are characterized by excessive waiting times at border crossings, inefficient procedures, overlapping responsibilities and insufficient coordination in terms of border management and inland enforcement, organizational and staffing shortcomings, inadequate infrastructure and excessive logistical costs for exports, imports and transit transactions which force local companies to carry excess inventories, in order to ensure timely deliveries. Corruption is also a major concern. The Customs Administration is perceived as one of the most corrupt institutions in FRY, with frequent requests for petty payments. A recent survey in Serbia indicated that 84 percent of respondents considered that there was "much" or "very much" Customs corruption and that 75 percent considered that the majority of Customs officials were involved.

The current legislation limits the role of Customs essentially to revenue collection activities and is not flexible enough to allow adaptation to rapid changes in traffic or functions. Many of the

procedures in place do not enable the FCA or the MCA to perform the duties of a modern Customs administration. Adaptation to a modern market economy that relies on enhanced regional integration and participation in the global economy will require significant procedural and operational changes to take place as soon as feasible.

Company Law: In the area of registering companies, Yugoslav tradition runs counter to Western norms, treating registration as evidence of the government's approval of the company's right to exist, rather than the Western idea of registration as public notice that the owners claim the protection of company law (as in the case of a limited liability company). The process of company registration is hugely time-consuming, overburdened as it is with required approvals, notifications, registration, fees and administrative discretion, which undoubtedly hinder foreign investors more than domestic ones. Simplification of the process of establishing a company would mark a major improvement in the business and investment climate.

The present federal **Law on Companies** (1996) establishes four well-known company structures, and two other forms: i) private limited liability companies, ii) joint stock companies (stock society), iii) partnerships, iv) limited partnerships; v) public company; and vi) socially owned-company. The latter, a uniquely Yugoslav construct, establishes the claim of employees and society regarding the ownership and management of the company. The Law provides that the government (federal or republic) is authorized to assume control over such a company, if the Federal State or one of its member republics is its founder, under certain conditions set out in republic laws.

Montenegro has adopted a separate **Companies Law** which has greatly simplified the procedure of establishing a company, allowing the registering by electronic means (Internet), a novelty in FRY. A new Law on Digital Signature and an Electronic Communications Law have been drafted but not yet adopted, though their enactment will be necessary for the full functioning of the Law on Companies.

Foreign Investment Legislation: The legal framework for foreign investment is regulated by the new **FRY Law on Foreign Investment** (OG FRY No.3/2002), which addresses issues including forms of foreign investment; the rights of foreign investors and their protection; incentives; contracts and other documents serving as the foundation of an investment activity; registration of companies; settlement of disputes; and penal provisions. Compared to the 1994 law, this new law liberalizes foreign investment in several respects, including by reducing the procedure for incorporation of foreign-owned companies to national treatment and by minimizing the requirement for reciprocity with other countries, an earlier Yugoslav approach which is at odds with the "most-favored nation" (MFN) notion at the core of the General Agreement on Trade in Services (GATS). Montenegro has enacted the same type of investment law as the FRY Law, but without the reciprocity provisions.

Competition Law: The laws regulating competition (FRY Anti-Monopoly Law of 1996, the FRY Law on Trade of 1993, and the FTT Law of 1992) do not adequately address competition issues and constitute a fragmented and vague framework, which is difficult to apply in a consistent fashion and falls short of international standards, including the OECD Guidelines. The paucity of the legislation in this important area is exacerbated by the weakness of the regulatory institution, the Anti-Monopoly Committee under the FRY Ministry of Economy and Trade, which was formerly a price-setting and market control unit. To date, it has focused its activities on attempting to set "fair" prices, rather than on policing unfair practices. It is now widely recognized within all levels of government in Yugoslavia that new law on competition is urgently needed, in particular to address merger control issues.

Taxation: Taxation systems in the FRY are in need of comprehensive reform, including the enactment of a consolidated law on tax administration and re-organization of revenue authorities. Actual tax administration in the FRY is at variance with the federal design. The republican governments in Montenegro and Serbia, which constitutionally possess power to tax, have suspended application of the Federal Foundations of the Tax Systems Act. Differences in taxation policy between the two republics have arisen and Montenegro no longer contributes to the federal budget. In Serbia, unification of sales tax rates represents an important reform.

Intellectual Property: Industrial property protection has a long tradition in Yugoslavia, based on membership of the Paris Union since its foundation in 1883. Industrial property laws are harmonized with the new legislation of EU and a new copyright law has been enacted. Yugoslavia has adopted a package of new intellectual property (IP) protection laws aimed at harmonization with EU law: Law on Patents, Law on Trademarks, Law on Models & Designs, and Law on Geographic Designations of Origin, all of which became effective in March 1995. A new Law on Copyright and Related Rights was enacted in May 1998. The FRY participates in various international conventions dealing with intellectual property rights. Because the Constitution of Yugoslavia (Art 16) provides that ratified conventions are part of internal legislation of Yugoslavia, the courts and other authorities apply the conventions directly and foreign nationals may require direct application of conventions at any time. Enforcement of industrial property laws has problematic areas, in particular with regard to computer software, video movies and music recordings, pirated copies of which are on sale in the streets of Belgrade and Podgorica. The capacity of the Federal Intellectual Property Office needs to be upgraded significantly.

Commercial Disputes: Commercial disputes are adjudicated in specialized commercial courts. There have been a number of problems with the enforcement of commercial judgments. The old **Law on Executive Procedure** established prolonged and cumbersome procedures which favored the debtor. Courts often refused to enforce judgments and the police, at the instruction of the political authorities, refused to execute court orders. A new Law on Execution Procedure, enacted in 2000, provides for the execution of final decisions issued by courts and arbitral or administrative bodies. Under certain conditions, it allows for execution upon presentation of commercial documents. The court can order the sale of personal or real property, the seizure of funds in a bank account, the assignment of an obligation to deliver goods, or the establishment of a security interest in property. While the new law shortens and expedites procedures, the courts are still unfamiliar with its provisions.

Arbitration: Another significant area of needed law reform is a modern legal framework for arbitration that meets international standards. The other main component of a legislative framework for arbitration – a statute governing procedural aspects of arbitration in the FRY – has not yet been enacted at any level in the FRY, even though the FRY is a party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958). In some federal states, such legislation has been enacted at the federal as well as at the republic levels (e.g., Canada and Australia). That gap, which an increasing number of jurisdictions have filled by enacting legislation based on the UNCITRAL Model Law on International Commercial Arbitration, hinders the development and practice of arbitration in the FRY. Experience on recent international tenders financed by IFIs in Yugoslavia, including on those financed by EBRD, suggests that the absence of credible arbitration rules and institutions acts as a significant deterrent to foreign bidders, who are dissuaded from bidding on such tenders because they fear that any arbitration proceedings which might be held in Yugoslavia would not consider their interests fairly.

Concessions: The legal regime governing concessions in Yugoslavia exists at two levels, federal and republican. At the federal level, Article 5 of the new Foreign Investment Law (Official Gazette of FRY, 3/2002) defines a concession only in its regular meaning, leaving the regulation to the Republics. According to this article, a foreign company may be awarded a concession for the exploitation of natural resources, goods in general use, and performance of activities in general interest. Also, a Build-Operate-Transfer (BOT) contract may be entered into for a specified facility, installation or infrastructure assets or communication facilities.

At the republican level, both Serbia and Montenegro have separate Concession Laws, published respectively in the Official Journal of Serbia 20/97, 22/97 and in the Official Journal of Montenegro 13/91, 10/96.

Serbia: According to the Serbian law, concessions may be granted to a domestic or a foreign person on the basis of a concession contract. Build-Operate-Transfer (BOT) arrangements are also specifically mentioned. The Serbian Concessions Law sets out a more detailed framework for concessions than does the federal law and lists sectors where concessions are allowed including oil, gas, mineral and telecommunications. Presently, draft amendments to the Serbian Concession Law are being considered, which are expected to extend this list to include other sectors, such as postal services. According to the Law, a foreign concessionaire has to establish a local vehicle for the performance of the activity being the subject of the concession. While the maximum length of a concession is 30 years, it is proposed to extend this period to 50 years. The Law states that upon the expiry of the concession contract, the ownership of assets shall be transferred to the state per the conditions of the concession contract, thus limiting arrangements to BOT only types. The Law provides for a public tender as a means to select the concessionaire. According to the proposed amendments, the specific agency currently responsible for granting a concession will cease to exist and relevant sector ministries will directly handle the concession-granting process.

Montenegro: The Montenegrin Law, like the federal law, is more general in nature. Under a ruling of the Federal Constitutional Court of March 1996, the provisions in the Montenegrin law relating to the granting of concessions by the Government of Montenegro have been declared unconstitutional. Therefore, it appears that the Federal Foreign Investment Law governs exclusively the granting of concessions to foreign entities in Montenegro.

C.9.6 Commercial Procurement Practices

Private sector procurement practices vary according to company size, form of ownership, management structure and contract value. The majority of the privately-owned small and medium enterprises (SMEs) undertake their procurement on a purely entrepreneurial basis, whereby contracts are generally low in value, are negotiated directly, and the choice of supplier is driven by the availability of credit or the opportunity to barter. The larger private sector companies are now beginning to implement procurement strategies that are increasingly aligned with modern best practice. Some have recognized that procurement is a specialist function and have established procurement departments within their companies, staffed by dedicated specialists. These companies conduct procurement on a strategic basis, using a combination of competitive tendering, shopping, and direct negotiation. As Internet usage increases —Internet service was introduced only in 1997; by 2000, there were 400,000 users—the use of electronic purchasing has been on the increase, with some companies using the Internet for sourcing research or direct ordering. A few companies already have or are introducing computerized procurement management systems.

D. RECOMMENDED ACTION PLAN

This section recommends actions to address the weaknesses in the public procurement environment. The recommendations are comprehensive but not necessarily exhaustive, and are subject to discussion and agreement with the various authorities. The recommendations are grouped according to legislative reform, procurement procedures and practices, increasing accountability, organizational reform and capacity building.

D.1 Legislative Reform

As described in Section C.1.3 above, current enactments on public procurement at the level of the Federal State are inadequate and fail to provide a reasonable, rules-based framework for procurement by federal institutions. Recent constitutional developments and the still ill-defined institutional arrangements of the future **State Union of Serbia and Montenegro** make it difficult to formulate precise recommendations for legislative reform at that level. However, if, as seems likely, each institution of the state union will be governed by its own Act, **the CPAR recommends** that provisions on how each institution is to conduct public procurement should be contained in the Act applicable to each institution. It would clearly be desirable that the provisions in the acts should be homogenous, in order to promote uniformity of practice at the state union level. At a later date, when the constitutional arrangements for the state union have come into sharper focus and assuming that the state union is responsible for international economic relations, **the CPAR recommends** that a specific law on public procurement should be enacted at the state union level and that the laws of the two republics should be reasonably harmonized with it, in order to achieve a common public market and to facilitate alignment with the EU.

In order to improve transparency and value for money in the defense sector, **the CPAR recommends** the procurement of non-military goods, works and services undertaken by the defense forces should be made subject to civil procurement legislation.

In the Republic of Serbia, the CPAR recommends that the new Draft Law on Public Procurement should be passed and enacted, with amendments to specific terms as proposed in this report, particularly in the detailed treatment given this subject in the section on "Procedures, Practices and Application." The World Bank wishes to maintain a dialogue with the Government of Serbia about the development of the draft law, in order to ensure that it provides the most comprehensive framework possible for the future conduct of public procurement in the republic.

Once Serbia's new Law on Public Procurement has been enacted, **the CPAR recommends** that a comprehensive set of detailed implementing regulations should be put in place to underpin the new law and to clarify its application in key areas. In order to refine application further, **the CPAR recommends** that a comprehensive set of standard bidding documents for the procurement of goods, works and services, should be developed, consistent with the law and implementing regulations and their use made mandatory by public institutions governed by the new law.

In the Republic of Montenegro, **the CPAR recommends** that the implementing regulations and standard procurement documents, already drafted with Technical Assistance from USAID, should be introduced as soon as possible and their use made mandatory.

In order to address the identified weakness of current arbitration rules and institutions, **the CPAR recommends** that, for the time being, all contracts which are subject to international bidding should include arbitration clauses specifying UNCITRAL rules and that arbitration proceedings will be conducted at an internationally-recognized institution, rather than in Yugoslavia. In both Serbia and Montenegro, the CPAR recommends that early priority should be given to the enactment of new laws on arbitration, which are consistent with international standards, such as UNCITRAL, and to the establishment of credible arbitration institutions.

Given the need to harness public procurement to promote sound environmental practices by public procuring entities, the CPAR recommends that provisions requiring Environmentally Responsible Procurement (ERP) should be introduced into future procurement enactments, perhaps by means of a separate implementing regulation.

D.2 Procurement Procedures and Practices

This report has identified many practices in public procurement in Yugoslavia, at all levels of administration, which fall short of the standards of transparency, fairness and competitiveness which are in indispensable to a well-functioning public procurement system. The causes of these practices have many roots, some of which lie in the inadequacy of the current legislation, particularly at the federal level and in Serbia, while others lie in the legacy of the previous, unaccountable regime, the weakness of the control environment and the inadequate training provided to public officials in procurement. It is clear that improving procurement practices will require not only better legislation, but many changes in the way that public institutions operate when conducting procurement. The key recommendations for changes in this area are identified below:

- a public bid opening should be required for all competitive tendering methods. The draft RS Procurement Act should be amended to remove the option, currently given to procuring entities, to decide not to have a public bid opening;
- the assessment of bidders' qualifications should be separated from the evaluation of bids and conducting either in pre-qualification or post-qualification, but not as part of the process of bid evaluation. Qualification requirements, including documentary requirements, should be stated clearly and unambiguously in the procurement documents;
- for all tendering-based procurement methods, the minimum period allowed to bidders for the preparation of their bids should not be less than thirty days;
- in order to timely improve access by bidders to information on bidding opportunities, the Government of Serbia should launch a public procurement website, on which invitations to bid should be published. Bidding documents should also be made accessible on this website for bidders for reading. Announcement of the results of all tenders should be made mandatory and should be published on this website;
- for goods and works, the evaluation of bids should be done on the basis of objective criteria which may be quantified in monetary terms. Award of contract should be to the lowest evaluated, responsive bid;
- because it offers an opportunity for corruption, the practice of negotiating contract terms with the winning bidder should be kept to a minimum and should be specifically excluded in the case of tender-based procurement methods, where the contract should be awarded strictly on the terms and conditions offered in the winning bidder's bid;

- in order to build a genuinely "common market" on the territory of Yugoslavia, the practice of affording a margin of price preference to bidders from a specific region should be discontinued;
- in the draft RS Procurement Act, the range of available procurement methods should be extended to include a two-stage bidding method for large and/or complex works and a simple Shopping method should be added for low-value purchases. Also, a specific procurement method should be added for consulting services. With regard to the Negotiated Procedure in the draft RS Procurement Act, for conditions under which it may be applied should be clearly defined and its use should be made subject to PPO prior approval.
- in the examination and evaluation bids, the principle of substantial responsiveness should be clearly established, whereby bids containing minor deviations may still be considered substantially responsive and not rejected on frivolous grounds. Potentially confusing or conflicting notions, such as: "correct tender", "appropriate tender" and "acceptable tender" should be avoided, as they may cause confusion or be open to abuse;
- the provision that bids whose prices are within three percent of each other may be considered equivalent for evaluation purposes should be deleted from the draft RS Procurement Act;
- given the illiquidity of most local bidders and the high cost of obtaining bid securities locally, public procuring entities may consider permitting bids to be submitted without a bid security as an interim measure, until the financial resources of local industry are restored. However, in any instance where a bidder withdraws his bid or fails to sign a contract, he should be suspended from further participation in public tenders for an appropriate period.

D.3 Organizational Reform

Given the imminent constitutional changes awaiting Yugoslavia, detailed recommendations on the most appropriate organizational arrangements for public procurement at the new state union level are difficult to make at this time. As suggested above, **the CPAR recommends** that responsibility for the conduct of public procurement should be decentralized to each state union institution.

With respect to the future structure of the state union, it is currently envisaged that the union will have its own parliament, executive and five ministries, each of which will clearly need access to appropriate support functions, including procurement. The options for resourcing and locating these functions currently appear to be three (i) that each institution conducts its own procurement (ii) that a state union equivalent of the current federal Mutual Services Agency conducts procurement on behalf of all state union institutions or (iii) that state union institutions delegate the performance of procurement to institutions at the republic level, most probably in Serbia, given that greater capacity is likely to be built at that level. The second option would require that a state union institution should appoint the MSA to perform some of the functions vested in it by the institution's own founding act.

On the assumption that, in order to be effective, the state union will require its own institutions, familiar with its own laws and procedures and accountable to state union authorities, a choice between the first and second options would seem appropriate. Given that the requirements of the state union institutions for procurement services is likely to be modest in scale - for example, there is unlikely to be much expenditure on high-value capital construction projects at this level – a small, dedicated procurement service located in an MSA-type agency could well offer the best combination of cost and efficiency. By contrast, the option of delegating procurement implementation to republic-level institutions might introduce a degree of dependence unacceptable to officials at the state union level.

In the Republic of Serbia, the draft Procurement Law provides for the establishment of an independent Public Procurement Office (PPO) which will report directly to the Government.

This approach, which in other countries has resulted in the creation of an independent Office of Public Procurement, has been adopted in a number of countries in transition in Central and Eastern Europe and has worked reasonably well in places such as Poland (www.uzp.gov.pl), Lithuania (www.vpt.lt) and Slovakia (www.uvo.gov.sk), for example. The key feature of such an organizational model is the agency's independence, which is essential to enable it to ensure the application of the procurement law without being subject to political influence. Independence is also a prerequisite for such bodies to operate effectively when conducting administrative review of bidders' protests, a function typically assigned to such organizations. It must be realized, however, that such an approach is not without cost or risk. Usually, when first established, such agencies struggle to exercise authority over line ministries. They need strong and visible backing from top political leadership - usually the Prime Minister – in order to gain the authority which they need to function effectively.

Yet other countries have opted for the establishment of an independent Public Procurement Commission or Board, a model which is currently being tried in Turkey.

The new Serbian PPO will not be established until one year after the new law is enacted. In the interim, the Mutual Services Agency (MSA) is to perform its functions. To make this interim arrangement feasible, **the CPAR recommends** that the MSA should be strengthened as a matter of priority, in order to increase its capacity to perform these new functions. Specific measures should include: the preparation of specific internal instructions defining how each of the authorized functions in the draft law are to be performed; authority and responsibility for decision-making under the authorized functions should be clearly defined; MSA should dedicate adequate resources to perform the authorized functions (staff, office space, computing and telecommunications facilities), rather than try to absorb the additional functions into the existing organization; additional staff with specialized skills should be hired to perform the new functions; Technical Assistance should be provided to the MSA, to assist it performing its new, interim functions; and a migration plan should be prepared for the efficient of transfer of authorities from the MSA to the PPO, once the latter is established.

In order promote better value for money and counter abusive differential pricing by bidders bidding on municipal tenders, **the CPAR recommends** that municipalities should consider establishing purchasing consortia, in order to concentrate their purchasing power vis-à-vis local and foreign bidders, to achieve overall cost savings for member municipalities and organizations by pooling the procurement of common items, to improve purchasing performance through the professionalization of the purchasing function. In other countries, municipalities have achieved good results from such collaborative schemes. One pertinent example is the Eastern Shires Purchasing Organization (www.espo.org), a local authority purchasing and distribution consortium, formed in 1981 by the County Councils of Leicestershire and Lincolnshire in the United Kingdom. ESPO currently spends in excess of £200 million (US$300m) each year on the procurement of goods and services, which are supplied to over 14,000 member organizations at more then 19,000 individual customer delivery points. Another pertinent model for municipalities to examine is that of the International Council for Local Environmental Initiatives' (ICLEI) European Eco-Procurement Initiative (www.iclei.org/europe/ecoprocura/index.htm), which aims to combine the purchasing power of some 49 local public authorities across Europe and, thereby, to create cumulative demand for environmentally responsible or "green" procurement solutions through the operation of its "Buy It Green" Initiative (see also C.2.22).

In Montenegro, **the CPAR recommends that** the Public Procurement Commission (PPC) should be strengthened by increasing its staffing and infrastructure to enable it to perform its functions fully and effectively. The PPC should also benefit from Technical Assistance to help it develop its staff skills and operating methods.

D.4 Strengthening the Control Environment

As identified by the Country Financial Accountability Assessment (CFAA), functioning internal audit department in all public institutions are necessary to ensure that efficient and effective operations are being maintained and that applicable laws and regulations are followed. To that end, **the CPAR supports the recommendation of the CFAA** that Internal Audit functions should be established in major spending institutions in all three governments. In order to equip internal auditors to carry out their duties in respect of public procurement, internal audit staff should attend specialist training courses for public procurement officers (see below), and should have access to procurement and appropriate technical expertise on an as-needed basis. This access may require the hiring of short-term consultants to help deal accurately with the technical aspects of procurement audits.

Because there are currently no Supreme Audit Institutions (SAIs), **the CPAR recommends** that all levels of government, at the federal level, as well as in Serbia and in Montenegro, should use qualified independent auditors to carry out annual, sample-based audits of the procurement operations of major spending ministries and public enterprises.

In addition to internal and external auditing, the other key element for ensuring that public officials are held accountable for their decisions on procurement matters is to have an effectively functioning bid protest system. In Montenegro, the bid protest system seems to be working reasonably well, though it is still early and the efficacy of the mechanism will no doubt be improved by the strengthening of the PPC. In Serbia, current provisions for bid protest are wholly inadequate, falling well short of international good practice and EU legislation. Therefore, **the CPAR recommends** that the function of performing administrative review of bidders' complaints should be added to those of the Public Procurement Office (PPO) in the current draft RS Procurement Act and that the PPO, once established, should be resourced appropriately to perform this duty.

D.5 Training and Capacity Building

This assessment has identified that one of the key causes of weakness in the implementation of public procurement in Yugoslavia is the lack of specialists in the function and public officials who have received training in procurement. There is, therefore, clearly a huge need to train public officials in procurement.

It is, therefore, particularly welcome news that the Technical Assistance program currently being planned by the European Agency for Reconstruction (EAR) will contain a sizeable training component. It should be kept in mind that training should take place within a well-planned, systematic and comprehensive framework. This is essential, not only to improve the quality of procurement carried out by public officials but also to underpin the effective implementation and success of the planned procurement reform program. To that end, **the CPAR recommends** that the RS MSA should develop a training strategy for public procurement, which should cover all levels of administration in Serbia and should take as its central objective the creation of a training

system which is itself sustainable over the long term. Assistance to the government with the development of such a training strategy might form part of the EAR's Technical Assistance. At a minimum, this strategy should define the numbers, grades, employing institutions and locations of public officials to be trained, make recommendations for a national curriculum for procurement training and for core content of training courses. It is important that customized short courses on the importance and key principles of good procurement management be provided to senior government officials and that a graduated suite of more technical courses should be delivered to practitioners.

In order to promote the establishment of a sustainable training system for public procurement, **the CPAR recommends that** a number of educational institutions in key centers be identified which will set up and deliver the agreed curriculum for public procurement training. Universities and technical colleges should be encouraged to include project management and procurement modules in technical courses, for example, in undergraduate engineering programs and in Masters of Business Administration courses, particularly those focusing on public-sector management.

Once this national training program for procurement has been established and operational for some time, **the CPAR recommends that** requirements should be introduced that only staff who have successfully completed the required training would be eligible to fill dedicated procurement positions in the public service and to serve on evaluation committees.

In Montenegro, procurement training capacity has already been built in the Faculty of Law of the University of Montenegro and a first round of courses has been delivered to central government officials. In order to improve further the capacity of the public administration, **the CPAR recommends** that procurement training courses should be conducted for public officials at local government level.

In order to assist the Faculty of Law to deepen the training program in procurement, **the CPAR recommends** that the Faculty should seek to establish twinning relationships with one or more Western European professional or educational institutions, with well-developed procurement curricula. This would enable the Faculty to develop its curriculum, upgrade the procurement training of its staff and enhance its ability to deliver training which is aligned to the EU Procurement Directives.

Once Serbian training institutions for public procurement have been identified, **the CPAR recommends** that these should join the twinning arrangement entered into by the Faculty of Law of the University of Montenegro, in order to facilitate the development of a public procurement training curriculum which is reasonably consistent across the two republics.

In addition, given that it is unlikely that the state union institutions will be able to provide dedicated resources to train their own staff engaged in procurement, **the CPAR recommends** that state union public procurement officers should be able to benefit from training at the Serbian training institutions.

In order to promote the professionalization of procurement as an occupation, recognized in its own right, governments in both republics should encourage the establishment of a national association or institute for qualified procurement managers and buyers. This institute should be open for membership to procurement staff working in both the public and private sectors. Membership would provide recognition that an appropriate level of professional qualification and experience had been reached. The association would promote, among other things, the application

of modern best practice, sound ethical standards and continuous professional development of its members.

D.6 Measures to be Taken by the Government

It is clear that the primary responsibility for implementing the planned procurement reforms lies with the Yugoslav authorities at the federal level and in both republics. In particular, it is for the Government of Serbia to enact the Draft Procurement Act, including the amendments recommended in this report, and to ensure that the institutional architecture to underpin the new public procurement system is put in place in a timely and adequately resourced manner. This will include equipping the MSA to perform the authorized functions under the new law and establishing the PPO promptly, as foreseen in the draft Act.

Likewise, implementation of the Action Plan presented with this report is primarily the responsibility of Governments at the level of the Federation and both republics.

D.7 Measures to be Taken by the Bank and Other Financiers

Now that the findings and recommendations of this report, as well as the Action Plan appended at Annex F, have been agreed between the Governments and the Bank, it is intended that this Final CPAR will form the basis of future procurement reform in Yugoslavia and in the State Union of Serbia and Montenegro. It is the Bank's intention to publish and disclose the CPAR in accordance with the Bank's disclosure policy, unless the Governments state their objection.

The finalization of the CPAR should, however, be seen by all parties concerned not as an end-point, but as the beginning of a process. Based on the Bank's experience in other countries, it may take several years to implement procurement reform successfully. Even when the first reforms have taken hold, continuous development will still be required, especially if Yugoslavia is to follow its stated path of harmonization of its legal environment with that of the EU. Throughout this process, the Bank will maintain an active dialogue with the authorities at all levels, through follow-up missions, to promote effective reform of public procurement and will provide technical assistance, if required. The Bank will also make its legal and procurement staff available to review and provide comments on draft laws, implementing regulations and bidding documents.

In order to promote the governments' ability to implement procurement according to the World Bank's procurement guidelines, the Bank should conduct a first procurement training seminar for the staff of implementation agencies responsible for Bank-financed projects in the upcoming fiscal year (FY03 = July, 2002 - June, 2003).

D.8 Technical Assistance

The governments at all levels will need substantial Technical Assistance to implement this reform program in a timely and effective manner. The World Bank estimates that to meet the needs of all levels of administration and to provide for the strengthening of recently established and new institutions, such as the RM PPC and RS PPO, approximately fifty staff-months of input would

be required over the next three years, which would require a financial outlay in the region of US$1.25 – 1.50 million.

The European Agency for Reconstruction (EAR) is currently preparing a Technical Assistance program for public procurement reform in Serbia, with an indicative value of €600,000 (US$581,500), which is an appropriate sum to cater for the short-term TA needs of Serbia but which, clearly, will not be sufficient to meet the entire requirements of all levels of administration over the life of the proposed reform period. The EAR and the World Bank are in active discussion about the design and content of the Terms of Reference for this TA, a copy of the Final CPAR has been shared with EAR and it is intended by both institutions that the TOR for the EAR TA will draw directly on the findings and recommendations of the CPAR.

The needs to be addressed by Technical Assistance are different at different levels of government. In Montenegro, given that the republic has already benefited from substantial TA financed by USAID, the needs now are primary for detailing the new law through implementing regulations, cementing good practice by the promulgation of standard bidding documents, improving enforcement by strengthening the Public Procurement Commission and building capacity through training public officials and building long-term training resources.

At the federal level and at the level of the planned state union, the current state of transition makes to difficult to calculate Technical Assistance needs accurately, as the size, functions and resources of the institutions of the new level have yet to come into focus. Assuming that these new institutions will perform their own procurement on a decentralized basis, they will certainly need TA in that regard. At a minimum, there is likely to be a need for assistance with the provision of procurement training.

Financing to meet these TA needs could come from one of a number of sources. The Bank encourages the Government to consider public procurement reform as a component under the Public Expenditure Capacity Building Project for Serbia, to be financed by the Bank and due to be appraised during 2002. In addition, the Bank may be able to assist the Government to identify potential sources of counterpart funding for this purpose.

D.9 Timetable

A time-bound Action Plan, covering the main recommendations made by this report, that appears as Annex F to this report.

D.10 Dissemination

Given the high level of interest among the general public, business sector and NGOs in the topic of public procurement reform, it is important that the governments at all levels and the World Bank should develop a clear dissemination strategy for this report. It is planned that the dissemination activities for this report will include:

- posting the final CPAR in electronic format on the websites of the Federal Government, Government of Serbia and on the Public Procurement in the Republic of Montenegro website. When the Serbian PPO launches its own website, the report should also be posted there;

- post the report on the websites of the World Bank and EBRD;

- hold a public conference to launch the EAR TA program to Serbia, at which the World Bank would be prepared to make a presentation on the basis of this report.

D.11 Monitoring and Follow-up Plan

The key institutions which will bear responsibility for monitoring the Action Plan and ensuring follow-up are the Federation/State Union Government, the Serbian MSA and the yet-to-be-established Public Procurement Office and, in Montenegro, the Public Procurement Commission. The EAR and World Bank, as the principal external partners interested in the development of the public procurement system, will also have a role to play in monitoring progress achieved by the governments against Action Plan. The development of a detailed set of indicators of the performance of the public procurement system, together with a plan for collecting the necessary data, should form part of the future TA provided to Yugoslavia.

ANNEXES

ANNEX A: CURRENT COMPOSITION OF WORLD BANK PORTFOLIO IN YUGOSLAVIA

No.	Sector	Grant / Credit Name	Effectiveness Date	Closing Date	Amount (US$M)	Amount Disbursed (US$M)
P074127	Private & Financial Sectors Development	Financial Sector Development	Oct. 2001	Jun. 2004	6.0	1.25
P074145	Private & Financial Sectors Development	Private Sector Development	Oct. 2001	Dec. 2002	6.0	0.48
P074136	Infrastructure / Energy	Emergency Electric Power Reconstruction	Nov. 2001	Jun. 2003	6.0	1.52
P074124	Human Development	Social Protection Economic Assistance	Nov. 2001	Dec. 2002	10.0	9.20
P074618	Infrastructure / Energy	Montenegro Environmental Infrastructure	Apr. 2002	Sep. 2004	2.0	0.0
P074586	Poverty Reduction & Economic Mgmt.	Structural Adjustment Credit (Serbia)	Mar. 2002	Aug. 2002	70.0	0.0
P074486	Private & Financial Sectors Development	Private/Financial Sector Structural Adjustment Credit	Not yet effective	June 2003	85.0	0.0
P075189	Human Development	Serbia Education Improvement Project	Not yet effective	Dec. 2006	10.0	0.0
P074090	Infrastructure / Energy	Trade and Transport Facilitation in Southeastern Europe	Not yet effective	Sep. 2006	6.5	0.0
Total:	**9 Operations**				**201.5**	**12.45**

ANNEX B: CURRENT COMPOSITION OF EBRD LOAN PORTFOLIO IN YUGOSLAVIA AS OF MARCH, 2002

Operational Sector	Industry Sector	Board Approval date	Facility Signing Date	Amount (€000)	Disbursed (€000)
Public	District Heating	7/24/01	07/27/01	20.00	0
Public	Municipal Services	7/24/01	07/27/01	20.00	0
Public	Municipal services	7/24/01	07/27/01	20.00	0
Public	Municipal Services	12/11/01	01/10/02	6.00	0
Public	Municipal Services	12/11/01	01/10/02	5.00	0
Public	Power Distribution	10/23/01	10/25/01	100.00	0
Public	Rail Transportation	10/23/01	10/25/01	57.00	0
Private	Depository Credit	12/18/01	02/28/01	1.31	0
Private	Depository Credit	12/18/01	02/28/01	0.838	0
Private	Depository Credit	09/04/01		61.00	0
Private	Plastics and Rubber Products	09/15/98	04/05/01	0.25	0
Private	Non-Metallic Mineral Product	09/15/98	04/09/01	0.25	0
Private	Tourism	09/15/98	11/12/01	0.13	0
Private	Health Care	09/15/98	07/30/01	0.20	0
Private	Manufacturing	11/06/01	03/01/02	0.25	0
Private	Furniture and related Products	11/06/01	02/06/02	0.25	0
Private	Equity funds	11/06/01	06/06/02	0.65	0
Private	Depository Credit	09/18/01	10/19/01	0.20	0
Private	" "	09/18/01	10/17/01	1.05	0
Private	" "	03/13/01	03/28/01	2.27	2.00
Private	" "	03/13/01	04/10/01	6.88	0
Private	" "	12/04/01	01/16/02	5.00	0
Private	" "	12/04/01	01/16/02	5.00	0
Private	" "	01/12/99	12/21/01	0.56	0
Private	" "	01/12/99	01/31/02	0.60	0
Private	Plastics and Rubber Products	11/20/01	11/28/01	4.00	1.79
Total			**26 projects**	**318.68**	**3.79**

ANNEX C: LIST OF ENACTMENTS RELEVANT TO PUBLIC PROCUREMENT IN THE FEDERAL REPUBLIC OF YUGOSLAVIA
as of May 13, 2002

Federal Enactments

TYPE OF ENACTMENT	REF. NO.	TITLE	DATE	AMENDMENT(S)	DATE
Law	Official Gazette of FRY no. 41/93	Property of FRY *(Zakon o imovini SRJ*)		OG of FRY, nos.24/94, 28/96, 30/98, 30/00	
Law	OG of SRY", br. 46/92,	Foreign Trade Transactions – *(Zakon o spoljnotrgovinskom poslovanju)*		OG of FRY, no. 49/92, 16/93, 24/94, 28/96, 29/97, 59/98, 44/99, 53/99, 55/99, 73/00, 23/01	
Regulation	OG of SFRY no. 62/81	Regulation on terms and conditions for procurement, usage, maintenance, keeping, and protection of objects of artistic and cultural value which are in use by Federal bodies *(Uredba o nacinu i uslovima pribavljanja, korišcenja, održavanja, cuvanja i zaštite predmeta umetnicke i kulturne vrednosti koje koriste savezni organi)*		OG of FRY no, 11/97	
Regulation	OG of SFRY, no.25/ 81	Regulation on terms under which transportation vehicles which are not manufactured in SFRY may be obtained for the needs of Federal bodies *(Uredba o uslovima pod kojima se sredstva prevoza koja se ne proizvode u SFRJ mogu nabaviti za potrebe saveznih organa)*			

Republic of Serbia Enactments

TYPE OF ENACTMENT	REF. NO.	TITLE	DATE	AMENDMENT(S)	DATE
Law	OG of Republ-ic of Serbia, no53/95	Law on Assets in Ownership of Republic of Serbia *(Zakon o sredstvima u svojini Republike Srbije)*		OG of RS, no.3/96, 54/96, 32/97, 44/99	
Law	OG of RS, no. 44/95,	Law on Construction of Objects *(Zakon o iygradnji objekata)*		OG of RS, no. 24/96, 16/97, 43/2001	
Law	OG of RS, no. 20/97,	Law on Concessions *(Zakon o koncesijama)*		OG of RS, no.22/97, 25/97	
Law	OG of RS, no. 44/95	Law on Construction Land *(Zakon o gradjevinskom zemljistu)*		OG of RS no.16/97, 23/01	
Law	OG of RS, no. 44/95	Law on Mining *(Zakon o rudarstvu)*			
Rules	OG of RS, no.27/97	Rules on terms, mode and procedure of granting approval for construction of objects - *(Pravilnik o uslovima, nacinu i postupku za ustupanje izgradnje objekata)*			
Rules	OG of RS, no.25/99	Rules on terms, mode and procedure for granting approval for development of technical documentation, for works on construction, reconstruction, maintenance, protection of highways, regional roads, and procurement of equipment and devices for the needs of roads or road object - *(Pravilnik o uslovima, nacinu i postupku za ustupanje izrade tehnicke dokumentacije radova na izgradnji, rekonstrukciji, odrzavanju, zastiti magistralnih i regionalnih puteva i nabavci opreme i uredjaja za potrebe puta ili putnog objekta)*			
Rules	OG of RS, 40/01	Rules on joint medical procurement of health institutions - *(Pravilnik o zajednickom medicinskom snabdevanju zdravstvenih ustanova)*			

REPUBLIC OF MONTENEGRO

TYPE OF ENACTMENT	REF NO.	TITLE	DATE	AMENDMENT(S)
Constitution	Sl.list RCG 48/92 OG of Montenegro 48/92	Constitution of the Republic of Montenegro *(Ustav Republike Crne Gore)*	10/12/92	
Declaration	Sl.list RCG 39/91 OGRM 39/91	Declaration on the Ecological State of RM *(Deklaracija o ekološkoj državi Crnoj Gori)*	9/20/91	
Law	44/99-2	Property of RM *(Zakon o imovini Republike Crne Gore)*		
Law	23/96-1	Privatization of Property Act *(Zakon o privatizaciji privrede)*		6/99-1,59/200-1
Regulation	25/99-1	Sale of shares and property of a company on a public auction *(Uredba o prodaji akcija i imovine preduzeca putem javne aukcije)*		42/99-1,18/2000-1
Regulation	8/99-7	Privatization funds *(O privatizacionim fondovima)*		18/2000-1
Regulation	8/99-4	Sale of shares and property by a public tender *(O prodaji akcija i imovine putem javnog tenderas)*		31/2000-1
Regulation	18/97-1	Control of the change of property of capital *(O kontroli promjene vlasništva kapitala)*		
Law	2/92-25	Property and management transformation *(Zakon o svojinskoj i upravljackoj transformaciji)*		27/94-389,27/94-391, 30/94-422, 23/96-1 Deleted from the law: article 7 subsection 2,article 42.st.2i article 43a and Chapter Gratuitous cession of capital by vouchers, articles 61,62 i 63.of the Law
Regulation	22/92-345	Procedure for identification of the state capital in companies *(Uredba o postupku za identifikaciju drzavnog kapitala u preduzecima)*		8/93-139 deleted item 4 of the Regulation

TYPE OF ENACTMENT	REF NO.	TITLE	DATE	AMENDMENT(S)
Guidelines	27/92-422	For the implementation of Regulation on the procedure for identification of the state capital in companies *(Za sprovodjenje Uredbe o postupku za identifikaciju drzavnog kapitala u preduzecima)*		17/93-281 deleted item 4 of the Regulation
Law	57/2000-2	Property of former socio-political organizations *(Zakon o imovini bivsih drustveno-politickih organizacija)*		
Law	14/92-195	Public expenditures *(Zakon o javnim rashodima)*		
Law	3/92-76	Public Income Agency *(Zakon o poslovima javnih prihoda)*		3/94,42/94,13/96
Law	30/93-539	System of public income (Zakon o sistemu javnih prihoda)		3/94,42/94,1/96
Law	10/60-149	Partition of Republic of Montenegro in municipalities *(Zakon o podjeli Republike Crne Gore na opstine)*		6/65,17/65,6/70,45/90 ,23/95,
Regulation	58/2000-3	Establishment and work of RM missions abroad *(Uredba o osnivanju i radu predstavnistava Republike u inostranstvu)*		
Law	55/2000-1	Expropriation Act *(*Zakon o eksproprijaciji*)*		
Law	14/92-193	Restitution of agricultural land to former owners *(Zakon o vracanju ranijim vlasnicima poljoprivrednog zemljista iz drustvene svojine)*		
Law	55/2000-12	Land survey, cadastre and registering the rights on immovable property *(Zakon o drzavnom premjeru, katastru i upisima prava na nepokretnostima)*		
Law	28/77-398	Cadastre on installations and subterranean objects *(Zakonm o katastru vodova i podzemnih objekata)*		29/89,39/89,48/91,17/ 92,27/94
Law	27/75-356	Transactions of immovable property *(Zakon o prometu nepokretnosti)*		35/75,29/89,39/89,7/9 1,48/91,2/92,4/92,27/ 92
Law	13/91-187	Concessions *(Zakon o koncesiji)*		10/96

TYPE OF ENACTMENT	REF NO.	TITLE	DATE	AMENDMENT(S)
Law	11/90-153	System of social planning and on the Social plan of Montenegro *(Zakon o sistemu drustvenog planiranja i Drustvenom planu Crne Gore)*		
Law	46/92-799	Development fund of RM *(Zakon o Fondu za razvoj Republike Crne Gore)*		
Law	29/89-567	Procurement and use of resources for stimulating the technological development of RM *(Zakon o obezbjedjenju I koriscenju sredstava za podsticanje tehnoloskog razvoja CG)*		28/91-484
Law	16/95-194	Planning and regulating public spaces *(Zakon o planiranju i uredjenju prostora)*		22/95-299,10/2000-14
Law	16/95-202	Waters *(Zakon o vodama)*		
Law	14/92-199	Maritime goods *(Zakon o morskom dobru)*		27/94
Law	28/93-505	Mining *(Zakon o rudarstvu)*		27/94

ANNEX D: FUNCTIONS, DUTIES AND RESPONSIBILITIES OF THE REGULATORY BODIES FOR PUBLIC PROCUREMENT IN SERBIA AND MONTENEGRO

Planned Functions of the Public Procurement Office Republic of Serbia	Duties and Powers of the Public Procurement Commission Republic of Montenegro
• participates in the preparation of public procurement rules; • provides consulting services to contractor and bidders; • organizes training in public procurement; • cooperates with foreign institutions and experts in public procurement; • publishes and distributes technical publications; • drafts model tender documentation for the typical sorts of public procurement; • disseminates information on public procurement in other states; • systematically collects basic statistical data at contractor and maintain databases of important public procurement data; • prepares and participates in setting professional criteria for assessing individual types of expenses at public finance beneficiaries; • prepares uniform standards for establishing records of suppliers and their financial standing based on data concerning the contracts planned and implemented; • monitors public procurement; • cooperates with other state bodies and organizations, organizations for compulsory social insurance and territorial autonomy and local government bodies; • submits to the Government annual analysis of public procurement situation in the previous year with proposals for improvement; • performs other tasks, in accordance with the law.	***Duties:*** • safeguard national interest, in public procurement matters, having due regard to the regional and international obligations of the Republic of Montenegro; • provide Parliament with a periodic procurement assessment report as required under the Act; • give due consideration to complaints of suppliers and of public entities on procurement matters; • give due consideration to perceived and detected irregularities and mismanagement; • make decision on the application of the Act in cases of disputes between public entities; • approve and disseminate public procurement rules and standard forms; • recommend to the Government any change to the Act. ***Powers:*** • oversee the operation of the procurement activities undertaken by any public entity, project management units and of the departments responsible for Procurement and Public Works; • investigate complaints from suppliers and public entities, and propose remedial action; • investigate reported cases of irregularity and mismanagement, and propose remedial action; • make decision in case of disputes between public entities on the interpretation of the Act; • decide on procurement procedures in compliance with the Act.

ANNEX E.1: COMPARISON OF PRICES PAID ON EAR-FINANCED LOCAL TENDER WITH FEDERALLY AUTHORIZED PRICES, 2001

(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(I)	(j)	(k)	(l)	(m)
#	**Item Description**	**Package Size**	**Unit Price paid by EAR after local competitive bidding (Euro)**	**Unit Price including distribution mark-up payable to pharmacies (+3.9%)**	**Wholesaler Unit Price as per FRY Official Gazette (YuD)**	**Wholesaler Unit Price as per FRY Official Gazette (Euro at Euro 1.00 = YuD 60.0297)**	**Unit Price Difference in Euros (e) - (g)**	**Percent Difference in Unit Price (h)/(e)[1]**	**Quantity of items purchased by local tender**	**Total Price Difference (h)*(m)**	**Total paid by EAR (Euro) (e)*(m)**	**Total Price for same quantities at FRY Official Gazette Prices (Euro) (g)*(m)**
1	Salbutamol spray 100mcg/dosa 200dosa	1	1.6300	1.6936	83.00	1.3826	0.3109	18.36%	75,000	23,319.08	127,017.75	103,698.67
2	Salbutamol sol 10ml (5mg/ml)	1	0.6400	0.6650	60.00	0.9995	-0.3345	-50.31%	200,000	-66,909.05	132,992.00	199,901.05
3	Amiodaron 200mg*	50	4.8600	5.0495	408.33	6.8021	-1.7526	-34.71%	30,000	-52,577.79	151,486.20	204,063.99
4	Atenolol 100mg	14	0.7000	0.7273	50.00	0.8329	-0.1056	-14.52%	300,000	-31,686.31	218,190.00	249,876.31
5	Captopril 25mg tab.	40	0.9300	0.9663	114.00	1.8991	-0.9328	-96.54%	237,000	-221,071.22	229,005.99	450,077.21
6	Digoxin 0,25 mg tab	20	0.3400	0.3533	26.00	0.4331	-0.0799	-22.61%	120,000	-9,583.07	42,391.20	51,974.27
7	Diltiazem 90mg tab.	30	2.0300	2.1092	140.00	2.3322	-0.2230	-10.57%	145,000	-32,336.29	305,829.65	338,165.94
8	Enalapril 20mg	20	1.3700	1.4234	145.00	2.4155	-0.9920	-69.69%	175,000	-173,607.18	249,100.25	422,707.43
9	Indapamid 2,5mg	30	0.8100	0.8416	139.00	2.3155	-1.4739	-175.14%	200,000	-294,786.10	168,318.00	463,104.10
10	Izosorbid mononitrate 20mg tab.	30	0.6540	0.6795	57.00	0.9495	-0.2700	-39.74%	178,000	-48,064.27	120,952.07	169,016.34
11	Izosorbid mononitrate 40mg tab.*	30	1.1950	1.2416	121.87	2.0302	-0.7886	-63.51%	102,000	-80,432.79	126,643.71	207,076.50
12	Nifedipin 20mg	30	0.6100	0.6338	50.00	0.8329	-0.1991	-31.42%	270,000	-53,765.38	171,123.30	224,888.68
13	Propafenon 150 mg	50	3.2610	3.3882	330.00	5.4973	-2.1091	-62.25%	33,000	-69,600.29	111,809.91	181,410.20
14	Verapamil 40 mg tab.	30	0.4900	0.5091	29.00	0.4831	0.0260	5.11%	44,000	1,144.70	22,400.84	21,256.14
15	Verapamil 80 mg tab.	45	0.9700	1.0078	80.00	1.3327	-0.3248	-32.23%	300,000	-97,453.10	302,349.00	399,802.10
16	Glibenclamid 5mg tab.	30	0.7000	0.7273	58.00	0.9662	-0.2389	-32.85%	191,000	-45,627.69	138,914.30	184,541.99
17	Gliklazid 80mg tab.	30	2.1400	2.2235	140.00	2.3322	-0.1087	-4.89%	307,000	-33,376.70	682,602.22	715,978.92
18	Insulin human intermediary acting 40UI/ml 10ml vial	1	5.2100	5.4132	311.00	5.1808	0.2324	4.29%	36,000	8,367.16	194,874.84	186,507.68
19	Insulin human rapid acting 40UI/ml 10ml vial	1	5.2100	5.4132	311.00	5.1808	0.2324	4.29%	13,000	3,021.47	70,371.47	67,350.00
20	Insulin lente spp 10ml 40iu/ml	1	3.3300	3.4599	261.00	4.3478	-0.8880	-25.67%	122,000	-108,333.29	422,104.14	530,437.43
21	Inutral spp 10ml 40UI/ml	1	3.3300	3.4599	261.00	4.3478	-0.8880	-25.67%	28,000	-24,863.38	96,876.36	121,739.74
								Total Price Difference:		**-1,408,221.49**	**4,085,353.20**	**5,493,574.68**
								Percentage Price Difference:		-25.63%		

(d): Actual price paid in Euros as a result of two local tenders financed by EAR in September and December, 2001.

(e): Price paid increased by wholesaler's margin of 3.9% to make prices directly comparable to prices published by the Federal Ministry of Internal Trade, which include wholesaler's margin of 6%
In the case of the EAR-financed tender, a local tender was also held between wholesalers, as a result of which their margin was reduced from 6% to 3.9%.

(f): Price published by Federal Ministry of Internal Trade pursuant to the Act on System of Social Control of Prices. This is the price which the RS Health Insurance Fund is authorized to pay.

[1] Prices paid by EAR vary from 18.36% over Official Gazette prices to 175.14% below OG prices. Of the 21 items cited, EAR prices were lower than OG in seventeen cases, and in the remaining four, EAR prices were higher than those of the OG. Overall, EAR prices are an average of 36.2% lower than OG prices.

ANNEX E.2: COMPARISON OF PRICES PAID FOR 46 DRUGS BY PHARMACIENS SANS FRONTIÈRES WITH PRICES PAID BY RS HEALTH INSURANCE FUND, MARCH-APRIL 2001

Drug Name	HIF Unit Price Paid April 2001 (YuD)	HIF Unit Price (USD) @65.00	PSF Unit Price Paid March 2001 (Euros)	PSF Unit Price March 2001 (USD)	Estimated Yearly Quantity [(a)]	Total HIF Yearly Cost (USD millions)	Total PSF Yearly Cost (USD millions)	Cost Ratio	Cost Difference (USD millions)
Albumin, human sol'n	25.704	0.395	0.431	0.392	1,200,000	0.475	0.471	1.008	0.004
Aminophylline 250mg/10ml	6.740	0.104	0.079	0.071	440,000	0.046	0.031	1.451	0.014
Amoxiciillin 500mg	5.500	0.085	0.071	0.065	9,600,000	0.812	0.622	1.306	0.190
Atenolol 100mg	5.714	0.088	0.036	0.032	28,000,000	2.462	0.909	2.708	1.552
Benzylpenicillin/procaine	7.000	0.108	0.196	0.179	3,200,000	0.345	0.571	0.603	-0.227
Captopril 25mg	2.850	0.044	0.115	0.105	41,600,000	1.824	4.349	0.419	-2.525
Carbamazepine 200mg	3.020	0.046	0.038	0.035	20,000,000	0.929	0.698	1.331	0.231
Ceftriaxone 1000mg	233.000	3.585	2.608	2.371	360,000	1.290	0.854	1.512	0.437
Cephalexin 250mg	7.000	0.108	0.070	0.064	9,600,000	1.034	0.611	1.692	0.423
Cephalexin 250mg/5ml	1.230	0.019	0.015	0.014	10,800,000	0.204	0.148	1.379	0.056
Diazepam 5mg	1.233	0.019	0.010	0.009	36,000,000	0.683	0.338	2.020	0.345
Diazepam 5mg/ml	13.100	0.202	0.715	0.650	1,600,000	0.322	1.040	0.310	-0.718
Digoxin 0.25mg	1.300	0.020	0.019	0.017	8,000,000	0.160	0.135	1.189	0.025
Diltiazem 90mg	4.800	0.074	0.094	0.085	9,600,000	0.709	0.820	0.864	-0.111
Dopamine 50mg/5ml	48.000	0.738	0.236	0.215	658,800	0.486	0.141	3.442	0.345
Doxycycline 100mg	6.600	0.102	0.068	0.062	2,000,000	0.203	0.124	1.643	0.079
Enalapril 20mg	13.850	0.213	0.105	0.095	23,600,000	5.029	2.253	2.232	2.776
Furosemide 20mg/2ml	11.300	0.174	0.056	0.051	10,400,000	1.808	0.529	3.415	1.279
Furosemide 40mg	2.300	0.035	0.042	0.038	4,000,000	0.142	0.153	0.927	-0.011
Glibenclamide 5mg	1.933	0.030	0.036	0.033	18,000,000	0.535	0.595	0.900	-0.059
Gliclazide 80mg	5.500	0.085	0.061	0.055	13,800,000	1.168	0.761	1.534	0.407
Ibuprofen 400mg	2.967	0.046	0.027	0.025	48,000,000	2.191	1.178	1.859	1.013
Immunoglobulin antitetanus 250mg/ml	537.000	8.262	9.800	8.909	36,000	0.297	0.321	0.927	-0.023
Indapamide 2.5mg	6.100	0.094	0.068	0.062	3,000,000	0.282	0.186	1.511	0.095
Insulin, human intermediary 40IU/ml	31.100	0.478	0.409	0.372	4,400,000	2.105	1.636	1.287	0.469
Insulin, human rapid acting	31.100	0.478	0.472	0.429	2,400,000	1.148	1.030	1.115	0.118
Ipratropium/Fenaterol inh.	464.000	7.138	6.500	5.909	160,000	1.142	0.945	1.208	0.197
Isosorbide MN 20mg	1.733	0.027	0.065	0.059	42,000,000	1.120	2.482	0.451	-1.362
Levodopa/benzarazide 250mg	9.110	0.140	0.162	0.147	4,000,000	0.561	0.589	0.952	-0.028
Maprotiline 25mg	2.067	0.032	0.033	0.030	3,600,000	0.114	0.109	1.049	0.005
Methyldopa 250mg	6.650	0.102	0.064	0.058	16,000,000	1.637	0.931	1.758	0.706
Metoclopromide 5mg	1.400	0.022	0.013	0.012	6,000,000	0.129	0.071	1.822	0.058
Metoprolol 100mg	4.067	0.063	0.060	0.054	12,000,000	0.751	0.651	1.153	0.100
Mexiletine 200mg	7.890	0.121	0.150	0.136	4,000,000	0.486	0.545	0.890	-0.060
Nifedipine 20mg	2.867	0.044	0.053	0.048	24,000,000	1.058	1.164	0.910	-0.105
Omeprazole 20mg	31.867	0.490	0.284	0.258	9,000,000	4.412	2.324	1.899	2.089
Ondansetron 4mg	164.600	2.532	4.533	4.121	168,000	0.425	0.692	0.614	-0.267
Paracetamol 120mg/5ml	0.450	0.007	0.010	0.009	48,000,000	0.332	0.415	0.802	-0.082
Paracetamol 125mg suppository	6.730	0.104	0.085	0.077	2,000,000	0.207	0.155	1.340	0.053
Pentoxyfilline 400mg	4.150	0.064	0.081	0.074	28,000,000	1.788	2.062	0.867	-0.274
Prazepam 10mg	3.050	0.047	0.064	0.058	2,160,000	0.101	0.126	0.806	-0.024
Ranitidine 25mg/ml	19.200	0.295	0.170	0.155	360,000	0.106	0.056	1.911	0.051
Ranitidine150mg	8.700	0.134	0.058	0.052	17,600,000	2.356	0.920	2.561	1.436
Salbutamol inhaler	83.000	1.277	2.670	2.427	200,000	0.255	0.485	0.526	-0.230
Tramadol 50mg	5.150	0.079	0.105	0.095	3,200,000	0.254	0.305	0.830	-0.052
Verapamil 80mg	1.778	0.027	0.021	0.019	12,600,000	0.345	0.244	1.410	0.100
Mean price		**0.617**		**0.614**		**0.962**	**0.778**		
Calculated Total Annual Cost						**44.268**	**35.775**		**8.493**
Percentage Difference								**23.7%**	

ANNEX F: ACTION PLAN

Actions	2002	2003	2004	Responsible Organization	Monitoring by	Indicators
I. Reform of Public Procurement Legislation						
Federation / State Union Level: Include public procurement rules in the Act applicable to each institution	**X**	**X**		Federation Government	Federation Gov't WB	Act on each institution passed
Make non-military procurement conducted by defense forces subject to civil procurement law	**X**			Ministry of Defense	Federation Gov't WB	Act governing MoD includes relevant provisions
Federation / State Union Level: Enact Public Procurement Law			**X**	Federation Government	Federation Gov't	Federal/State Union law enacted
Serbia: Enact draft Public Procurement Act, including amendments proposed in this report	**X**			RS Government, Parliament	RS MOFE EAR WB	Public Procurement Act comes into effect
Serbia: Adopt implementing regulations and promulgate standard bidding documents		**X**		RS MSA RA PPO	RS Gov't EAR WB	Regulations and bidding documents adopted
Montenegro: Adopt implementing regulations and standard bidding documents	**X**			RM PPC	RM Gov't WB	Regulations and bidding documents adopted
Both Serbia and Montenegro: Enact a new Law on Arbitration and arbitration rules. Establish arbitration institutions.		**X**	**X**	RS Government, RM Government	RS, RM Gov'ts WB	New laws enacted. Institutions established.
Federation/State Union Level, Serbia and Montenegro: Enact implementing regulations on Environmentally Responsible Procurement (ERP).			**X**	Federation, RS and RM Governments	Federation, RS, RM Gov'ts WB	Implementing regulations enacted. ERP provisions introduced into standard bidding documents.

Serbia: • Require public bid opening for all tendering methods • Assess bidders' qualifications separately from evaluation of bids. State qualification requirements clearly in procurement documents • Allow minimum bidding period of 30 days for all tender-based procurement methods • For goods and works, evaluation of bids should be based on objective criteria, quantified in monetary terms. Award contract to lowest evaluated, responsive bid • Delete provision that bids within 3 percent of each other on price may be considered equivalent • Abolish margin of price preference to bidders from specific regions • Extend range of procurement methods to include two-stage bidding method, Shopping method, a specific procurement method for consulting services • Make Negotiated Procedure subject to PPO prior approval • Introduce the principle of substantial responsiveness in bid evaluation.	**X**			RS MOFE	RS Government	Amendments made to current draft RS Public Procurement Act
Serbia: Launch public procurement website		**X**		MSA/PPO	RS Gov't EAR WB	Website launched
III. Reform of Organizations & Accountability of Public Officials						
State Union: Decentralize responsibility for public procurement to state union institutions		**X**		State Union Gov't	State Union Gov't WB	Provisions made in acts government state union institutions
Serbia: Strengthen RS MSA to increase capacity to perform regulatory functions	**X**			RS Gov't	RS Gov't EAR WB	EAR TA program provides capacity building to MSA. MSA performing functions satisfactorily

Serbia: Establish RS Public Procurement Office		**X**		RS Gov't	RS Gov't EAR WB	RS PPO established and performing functions satisfactorily
Montenegro: Strengthen Public Procurement Commission (PPC); increase staffing and infrastructure	**X**			RM Gov't	RM Gov't WB	PPC staffing, resources increased. PPC performing all functions effectively
Montenegro: Amend the Criminal Code to define a new offence of fraud and corruption related to public procurement	**X**			RM MoJ	PPC WB	Criminal code amended
Serbia: Amend the Criminal Code to define a new offence of fraud and corruption related to public procurement		**X**		RS MoJ	RS MSA/PPO WB	Criminal code amended
IV. Strengthening the Control Environment						
Federation/State Union. RS, RM: Establish Internal Audit functions in major spending institutions		**X**	**X**	State Union , RS and RM Gov'ts	All 3 Gov'ts WB	Internal Audit units established and functioning effectively.
Federation/State Union. RS, RM: Hire qualified independent auditors to carry out procurement audits of major spending institutions	**X**	**X**	**X**	State Union , RS and RM Gov'ts	All 3 Gov'ts WB	External auditors hired Audits conducted Audit reports completed
Serbia: Add administrative review of bidders' complaints to authorized functions of Public Procurement Office (PPO)	**X**			RS MOFE	RS Gov't EAR WB	Amendment made to draft RS Act
V. Training and Capacity Building						
Serbia: RS MSA/PPO to develop a training strategy for public procurement		**X**		MSA/PPO	RS Gov't EAR WB	Training strategy prepared and published
Serbia: Identify educational institutions to deliver public procurement curriculum		**X**	**X**	MSA PPO	RS Gov't EAR WB	Institutions selected Courses launched
Montenegro: Conduct procurement training courses for local government officials	**X**	**X**		Faculty of Law	PPC WB	200 officials trained
Montenegro: Establish twinning relationship between Faculty of Law and Western institution(s)		**X**	**X**	Faculty of Law	PPC WB	Twinning arrangements in operation

				Law		
Serbia: Establish twinning arrangements between Serbian educational institutions and counterparts in Western countries and Montenegro			**X**	Educational Institutions	RS PPO	Twinning arrangements in operation
Serbia: Training institutions to make services available to federal/state union public procurement officers		**X**	**X**	RS PPO Training institutions	RS PPO EAR WB	State union procurement officers attending training courses
Both Serbia and Montenegro: Establish a professional institute for procurement practitioners			**X**	RS Gov't RM Gov't	RS PPO RM PPC	Institute(s) established. Entry requirements set. First members admitted.

ANNEX G: COMMENTS ON THE DRAFT PUBLIC PROCUREMENT ACT OF SERBIA

Structure and Form

1. The outline of the draft law is neither clear nor logical. Principles that should be stated in the introduction and or in a preamble are found in subsequent provisions (e.g. Articles 5 to 8). There are many repetitions; provisions dealing with similar concepts (e.g. eligibility, Articles 6, 8, and 45) or procedures (e.g., negotiated and restricted tendering , Articles 22, 23, 52, 53, 70, 72, 73,93, 94 and 100-110) are scattered in many different places .

2. More important, the law, while invoking broadly accepted principles of fairness and transparency, fails to embody these principles in the detailed provisions of the text, and introduces many exceptions such as reciprocal access, restricted and negotiated tendering.

3. Certain provisions, such as those dealing with detailed contents of the bidding documents, the process to be followed to determine the contract value and rules applying to technical specifications do not belong in a law and should be addressed in implementing regulations. In short, a more streamlined law would certainly be more accessible to its users and would support more transparent practices. A Table of Contents would also help make the law easier to navigate.

Critical Deficiencies

1. There are several very major deficiencies in the draft law:

(i) Use of "Restricted Procedures", a combination of pre-selection, pre-qualification and standing pre-qualification, should be acceptable only for contracts of small value and for contracts for which there is only a limited number of providers of the goods or services. Standing pre-qualification - justified when there is no time to invite bidders to submit offers throughout a long period of time - to our knowledge is primarily used in conjunction with the procurement of crude oil.

(ii) Widespread Use of "Negotiated Procedures", with or without prior publicity, is foreseen in many other cases besides those listed in Article 23 (those ones are generally acceptable). One possible way to deal with such additional cases (see for example Article 102) would be to require exceptions to be specifically granted by the Public Procurement Office .

(iii) Lack of Transparency in the Selection of Providers of Services: (articles 98 to 105). This section on procurement of services should be modified to address specifically the selection and hiring of consultants (more or less what is found in Articles 100, 102 and 104) and provide for a procedure along the lines of the Bank's Consultant Guidelines "Quality and Cost-Based Selection." Article 101 should be dropped and the services governed by article 101 (to be defined as services contracted on the basis of measurable physical outputs) should be addressed in the section of the law dealing with open competitive bidding with or without pre-qualification.

(iv) Procurement of Public Utility Services Providers (articles 106 to 121). This section would have been immensely helpful, had it not attempted to mirror the EU Directive 93/38/EEC and, instead, had reflected the rules and practices followed in some

countries of Latin America (e.g. Brazil) , where public utility services are procured in accordance with open competitive bidding.

(v) Reciprocal Access ("Reciprocity") on the basis of equal treatment of another country's nationals, mainly through Article 96 (which provides for the Chamber of Commerce of the Republic of Serbia to draw "a list of interested providers of works" on the basis of preferential (international) agreements and Articles 118 , 119 and 120 (which exclude or suspend the award of contracts not going to preferred international partners. The effect of these two last series of provisions is to create a "club" of eligible bidders that will exclude bidders coming from other countries, in particular from Part II neighboring countries whose participation should, on the contrary, be encouraged.

Detailed Review

3. Other significant substantive or drafting deficiencies can be found in the articles examined below.

Article 13 provides for tender documents and proposals to be in the Serbian language and Article 14 provides for an exception without establishing the relevant criteria governing this exception. The tender documents should be available in English (or in another widely used language) when foreign bidders are expected to participate and bidders should be permitted to submit bids in the English language.

Article 18 provides for the creation of a Public Procurement Office. The mandate of the Office, set out in Article 19, should be expanded in order for it to prepare standard general conditions of contracts and it should also be the agency in which should be domiciled a bid protest review panel.

Article 22 See comment in par. 2 above.

Article 45 (paragraph 5) mentions that in order to be eligible to submit a bid (it should be to be awarded a contract), a bidder needs a "valid permit from the body responsible for the activity which is the subject of the contract, whenever such permit is required by a special regulation." It is not clear whether this is a reference to registration with a professional body, or the registration of a corporation and an arbitrary application of this provision may undermine open access to the bidding process.

Articles 52 and 53 (refer to see comments in par. 2 above)

Article 55 refers to the criteria to be used for bid evaluation. It should mandate that evaluation criteria be all disclosed and quantifiable in monetary terms. Article 55 following the model of the UNCITRAL model law also describes two ways of identifying the winning bidder. There should be only one, namely the award should be made to the lowest evaluated bidder.

Article 58 Clarifications should be provided in writing.

Article 60 : The time limit for submission of bids should be calculated from the date when bid documents are made available to the public.

Article 61 should state that the deadline for bid submission and bid opening date are the same (see also Article 77).

Article 68 provides for "additionally reduced time limits" to submit tenders, which are untransparent.

Article 69. In order to enhance the transparency of the process, advertisement should be made in a widely distributed newspaper and be posted on electronic media, such a website launched and maintained by the Public Procurement Office.

Article 77 specifies that tenders will be opened in public but does not indicate whether they will opened just after the deadline for bid submission. Public opening should be immediately after the closing date and time for the receipt of the tenders.

Article 77 provides exceptions to public opening of bids; some of these exceptions could be interpreted in ways which reduce transparency. Whereas some of these exceptions are legitimate or at least commonly found in procurement laws e.g. military or state secrets some others are unjustified e.g. trade secrets (in which case, one part of the bid could remained sealed),

Article 93 and 94 provide for negotiated procedures without publication or be used under specific circumstances, some of which are unjustified (repetitive construction works, R&D, for the purpose of development). Those contracts could be tendered by limited bidding or open bidding (with pre-qualification).

Article 96 (refer to comments above in par. 2 above)

Article 97 allows the employer to impose conditions relating to the obligations of subcontractors, which the bidder has to accept. This should be restricted to a few critical aspects of subcontracting, such as the qualification of the subcontractor and the certification of the services subcontracted.

Article 99 provides for a long list of exceptions to the law itself, some of which are hardly justified e.g. sub-par. 3, 4, 6, 9)

Article 100 to 102 (refer to comments in par.2 above)

Article 105 provides that the notice of award of services contracts shall be published in the Official Gazette not later than 48 days after the conclusion of the contract. This is much too late for a bidder to submit a bid protest in a timely manner (i.e. before the award is made final). Besides, it appears that some of the awards for services contracts listed in Annex 1B appear shall not be publicized.

Chapter V (refer to comments in par. 2 above)

Articles 134 to 143 The section on the bid protest review conducted by the Commission for Protection of Tenderers, although not very well drafted, remains one of the most satisfactory sections of the law, as the provisions are governed by some good principles: challenge of procurement procedure and of a specific award decision are possible, contract award is suspended, the decision of the Commission is final. However, the composition of the Commission needs to be more balanced and, in addition to

magistrates, should include representatives of professional bodies; also, it might be excessive to provide for both compensatory damages (for loss of future profit) to be awarded by the courts, and suspension of the award.

Article 144 provides for cancellation of contracts that have been awarded illegally but does not address compensation, if any, that would be due as a result to a supplier or service providers acting in good faith.. Penalties listed in Article 145 (to be paid pursuant to violations listed in Article 144 and perhaps other violations as well) should be also listed in the statutory rules governing public servants.

Article 146 provides for fines to be imposed on bidders having engaged in fraudulent conduct. It should also address (i) the mechanisms ensuring that determination of fraud was achieved in a fair manner, and (ii) black-listing that normally results from fraud.

Finally, we note that the draft law has few provisions related to contract matters (securities, liquidated damages, price adjustment) which are of critical importance when it comes to protecting the party contracting with the government entity.