

Screening report

Serbia

Chapter 17 – Economic and Monetary Policy

Date of screening meetings:

Explanatory meeting: 2 and 3 December 2014

Bilateral meeting: 12 March 2015

I. CHAPTER CONTENT

The *acquis* in the area of economic and monetary policy is governed by Title VIII (Articles 119 to 144) of the Treaty on Functioning of the European Union (TFEU), and by relevant implementing legislation. Treaty provisions related to the adoption of the euro do not apply to Member States with a temporary derogation as defined in Article 139 of the TFEU.

The *acquis* in the area of economic and monetary policy contains specific rules requiring the independence of central banks in Member States, prohibiting direct financing of the public sector by the central banks and prohibiting privileged access of the public sector to financial institutions. Member States shall regard their economic policies as a matter of common concern and are subject to fiscal and broader economic and financial surveillance. They are also obliged to adhere to detailed rules concerning the characteristics of their national budgetary frameworks. New Member States also need to comply with the criteria laid down in the Treaty in order to be able to adopt the euro in due course after accession. Until then, they will be a Member State with derogation from the use of the euro and shall treat their exchange-rate policies as a matter of common interest.

The *acquis* consists mainly of Treaty provisions and protocols as well as regulations and decisions that do not require transposition into national legislation. Nonetheless, as indicated in Article 131 of the TFEU, each Member State shall ensure that its national legislation, including the statutes of its central bank, is compatible with the TFEU and the Statute of the European System of Central Banks and of the European Central Bank (ESCB/ECB Statute). Regulations under this Chapter require Member States to identify potential risks, prevent or correct any excessive fiscal deficits and harmful macroeconomic imbalances. Directive 2011/85 lays down the requirements for the budgetary frameworks of Member States and requires transposition into national legal and administrative order.

II. COUNTRY ALIGNMENT AND IMPLEMENTATION CAPACITY

This part summarises the information provided by Serbia on its legislation and administrative capacity and the discussion at the explanatory screening meeting held on 2 and 3 December 2014 and the bilateral screening meeting held on 12 March 2015, as well as additional information provided thereafter.

Serbia indicates that it can accept the *acquis* regarding Chapter 17 'Economic and Monetary Policy'. It indicates that it does not expect any difficulties to implement the *acquis* by the time of accession.

II.a. Monetary policy

(i) Functional independence

Pursuant to Article 3 of the Law on the National Bank of Serbia, the primary objective of the National Bank of Serbia (NBS) shall be to achieve and maintain price stability. The secondary objective shall be contributing to the maintenance and strengthening of the stability of the financial system, while support to the pursuance of economic policy of the Government of the Republic of Serbia, operating in accordance with the principles of a market economy, is

considered a tertiary objective. The NBS is entitled to propose to the National Assembly the laws within its scope of competence.

(ii) Institutional independence

Serbia stated that the independence of the NBS is enshrined in the Constitution of the Republic of Serbia. The primary law that regulates the functioning of the NBS is the Law on the National Bank of Serbia (Law on the NBS). Pursuant to Article 5 of the law in question, the NBS has a distinct legal personality from the State. The law explicitly prohibits the NBS, the bodies of the NBS and the members of those bodies to seek or take instructions from government bodies and institutions, the National Assembly, or other persons. According to the law, Government bodies and institutions, and other persons may not threaten the autonomy and independence of the NBS nor seek to influence the NBS, its bodies, or the members of these bodies in carrying out their tasks.

According to Serbia, the NBS is autonomous in pursuing the dinar exchange rate policy and determines the dinar exchange rate regime with the consent of the Government. The NBS has the exclusive right to issue banknotes and coins in the Republic of Serbia and it can make a decision to issue commemorative coins and numismatic money at the initiative of the Government or at own initiative.

Serbia stated that the NBS is subject to the oversight of the National Assembly (through its reports, parliamentary hearings and parliamentary questions) and accountable to it for its work. Article 71 of the Law on the NBS clearly excludes ex-ante consultation with the National Assembly related to NBS's decision. An administrative dispute may be initiated against an administrative act of the NBS passed in the performance of its tasks, but an action against such act may neither prevent nor postpone its implementation and the court may not resolve an administrative matter the resolving of which is placed under the scope of authority of the NBS by Law.

The NBS, the Governor, Vice-Governors, Director of the Supervision Administration and other employees of the NBS are not liable for the damage caused in the performance of the NBS tasks, unless proven that they did not act in good faith.

According to Serbia, pursuant to Article 10 of the law, the NBS cooperates with the Government and other state bodies and, without prejudice to achieving its objectives, undertakes measures within its scope of authority to promote that cooperation. The relations between the NBS and the Government are regulated by the provisions of the Law on the NBS and a number of non-binding agreements. The minister in charge of finance is invited to attend the meetings of the Executive Board of the NBS, and could participate in deliberations without the right to vote.

Serbia informed that the NBS and the Government agreed, with a view to achieving price stability, that the NBS shall implement the inflation targeting regime. Pursuant to point 6 of the Agreement on inflation targeting, if the inflation target has been missed for more than six consecutive months, the NBS shall notify the Government in writing about the reasons for such departure, measures to be taken and the time needed for inflation to return within the target range.

(iii) Personal independence

According to Serbia, Article 19 of the Law on the NBS complies with the general requirement under Article 14.2 of the ESCB/EC Statute as regards the minimum five year period for the term of office of a Governor. The Governor, Vice-Governors and Director of Supervision Administration are appointed for a six-year renewable term of office. The Members of the Council are appointed for a five-year renewable term of office. The National Assembly appoints and dismisses NBS officials (the Governor, Vice-Governors, Director of the Supervision Administration, and members of the Council). The Governor is appointed upon a proposal of the President of the Republic of Serbia, Vice-Governors are appointed upon the proposal of the Governor, the Director of the Supervision Administration and the members of the Council upon a proposal of the National Assembly's committee in charge of finance (Finance Committee).

The reasons for dismissal of an official of the NBS are listed in Article 28 of the law. The reasons for the dismissal of the Governor, Vice-Governors and Director of the Supervision Administration should be examined by the Council, while the reasons for the dismissal of a member of the Council should be examined by the Finance Committee. An official may lodge against the decision on dismissal an appeal with the Constitutional Court within 30 days from the day that decision was published in the "RS Official Gazette".

Article 20 of the Law on the NBS foresees safeguards against conflict of interest of the Governor and his/her incompatibility of functions. This Article applies accordingly to the Vice-Governor, Director of the Supervision Administration and the Council members.

(iv) Financial independence

According to Serbia, the Republic of Serbia is the owner of the entire capital of the NBS. According to Article 73 of the Law on the NBS, the NBS uses assets of the Republic of Serbia for its operations. The Governor decides on the procurement and use of the assets, as well as on their management and disposal. The Government has the right to decide on the alienation of NBS immovable property and on establishing a mortgage on it. The NBS is not a subject to corporate profit tax, nor to any other direct taxes and court and other duties and fees from which state authorities and organisations are exempt.

Pursuant to Articles 23 and 74 of the Law on the NBS, the NBS has a financial plan setting out its revenues and expenditures planned for the following year. The Council adopts the NBS financial plan. The NBS submits, for information thereon, the financial plan for the following year to the National Assembly. The NBS law defines the minimum core capital and rules to allocate NBS profit (including profit from exchange rate differences and revaluation reserves) and to cover NBS losses. Upon reaching the minimum amount of core capital (RSD 10 billion) and the special reserve amount (RSD 20 billion), the profit not originating from exchange rate differences and revaluation reserves is subject to distribution - 10% to core capital, 20% to special reserves and 70% to the state budget.

Serbia stated that the NBS's annual financial statements are prepared in line with international accounting standards. The audit of the financial statements of the NBS is performed by an external auditor selected by the NBS in line with the law governing public procurement. An internal audit, overseen by the Council, is also performed. Pursuant to Article 10 of the Law on State Audit Institution, the NBS is also subject to the audit of the State Audit Institution but only for utilisation of public assets and transactions linked to the state budget. The Council submits the annual financial statements, along with the external auditor's report, to the National Assembly, for information thereon.

(v) Prohibition of monetary financing of the public sector

Pursuant to the Article 62 of the Law on the NBS, the NBS may not approve credits, loans, overdraft facilities or other forms of credit facilities to the Government of Serbia, the autonomous province or local government units, public enterprises and other legal entities funded or controlled by one of the above-mentioned. The NBS may not issue guarantees for the settlement of obligations of those entities or secure the settlement of their obligations otherwise, and may not directly purchase securities issued by said entities. Serbian legislation in this field prohibits the monetary financing of the public sector or of the public sector obligations to third parties, assumption of public sector liabilities, as well as bearing the costs of resolution funding. According to Article 38 of the Law on the NBS, the NBS may grant short-term emergency liquidity assistance but only to a solvent bank against adequate collateral. On the basis of law or contract, NBS may perform fiscal agent operations for the state as long as it does not threaten its autonomy and independence. NBS maintains the consolidated treasury account system, paying interest on these assets and charging fees for its operations.

According to Serbia, the Law on the NBS (Article 62) is aligned with the relevant provisions of TFEU, namely Article 123, and with Article 21 of Protocol 4 of the ESCB/ECB Statute with the exception of the definition of public sector in the EU and the Member States. As it currently stands, Article 62 covers the entire public sector in Serbia (the public administration, local self-government, other regional, local and public authorities, legal persons).

(vi) Prohibition of privileged access of the public sector to financial institutions

Serbia stated that the Law on Banks does not contain provisions that can be regarded as establishing privileged access. The prudential requirements, based on risk weights set forth in Basel II standards, do not provide preferential treatment for exposures to the Republic of Serbia or the NBS. Serbia further stated that Article 131 of the new Insurance Law does not provide any preferential treatment for securities and/or money market instruments issued by the Republic of Serbia. According to Serbia, the Law on Voluntary Pension Funds and Pension Schemes does not discriminate on the basis of different form of assets. The only difference in treatment is that Voluntary Pension Funds' assets may be invested in debt securities issued by the Republic of Serbia and the NBS, autonomous provinces and local government units in the Republic of Serbia and other legal entities with the guarantee of the Republic of Serbia without any limitations, whereas there are certain limitations for other categories.

According to Serbia, the provisions of the Law on Capital Market governing investment firms do not contain any incentives or restrictions that can be interpreted as establishing privileged access.

(vii) The integration of the national central bank into the ESCB

Serbia acknowledged that it is necessary to complement the Law on the NBS with the necessary provisions ensuring integration of the NBS into the ESCB and notably reflecting its subordination to the guidelines and instructions of the ESCB and ECB as from the date of euro adoption.

II.b. Economic policy

Serbia has been participating in pre-accession economic policy co-ordination since 2006 when it submitted its first Economic and Fiscal Programme to the Commission. From 2012, Serbia submitted a Pre-accession Economic Programme and since 2015 it submits an Economic Reform Programme (ERP). The ERP, both in its macro-fiscal framework and structural reforms part, is based to a large extent on the national Fiscal Strategy, which accompanies the annual draft budget when it is proposed to the National Assembly. In addition, it also presents an alternative macro-fiscal scenario, outlines the monetary policy stance, analyses external sustainability, and identifies key obstacles to growth and competitiveness.

(i) Budgetary surveillance

Serbia stated that pursuant to the Public Debt Law, public debt is an absolute and unconditional obligation of the Republic regarding repayment of principal, interest and other borrowing costs and is prioritised over other public expenditure. Serbia may borrow to cover its budget deficit, for liquidity purposes, to refinance public debt, to finance investment projects and to cover liabilities arising from issued guarantees. There are several definitions of government debt in different legal acts. According to the Public Debt Law, public debt of the Republic of Serbia consists of direct liabilities, arising from securities and agreements into which Serbia has entered, and guarantees issued by Serbia to local governments and legal entities founded by the State. According to Budget System Law, for fiscal rules purposes, general government debt includes non-guaranteed debt of local governments, but excludes potential restitution liabilities.

(i.1) Accounting and statistics

Statistical coverage and reporting in Serbia are regulated by the Law on Official Statistics. The legal framework in this field also includes the Programme of Official Statistics in the period 2011 to 2015 and the Plan of Official Statistics for 2015. The Programme of Official Statistics for 2016-2020 was adopted by the Assembly in June 2015. From September 2014 Serbia started to implement the European System of National and Regional Accounts (ESA) 2010 methodology. The calculation of Gross Domestic Product and other macroeconomic aggregates is carried out on annual and quarterly basis, applying production and expenditure approach, at current and previous year prices. Data series starting from 1995 are publicly available. Serbia has not yet started officially submitting fiscal notification tables to Eurostat. However, the Statistical office has assumed responsibility for compiling and sending excessive deficit procedure (EDP) tables and is coordinating the efforts of the Ministry of Finance and the NBS to improve government finance statistics and begin transmission of fiscal notification statistics on ESA 2010 basis.

(i.2) Macroeconomic and budgetary forecasts

Macroeconomic and budgetary forecasts are prepared by the Ministry of Finance, and in the case of inflation, exchange rate and balance of payments forecast in collaboration with the National Bank. Fiscal projections are made by the Ministry of Finance on the basis of envisaged economic policy, macroeconomic framework, public debt trends, planned changes in the tax policy and regulations for specific categories of expenditures. These forecasts are discussed twice yearly with the European Commission.

(i.3) Numerical fiscal rules

The numerical fiscal rules were introduced with the Budget System Law in 2010 (Article 27). According to them, the fiscal policy is to be conducted in a transparent, sustainable and responsible manner. The general government debt limit is set at 45% of the GDP, excluding the debt based on the Law on Restitution (restitution bonds of up to EUR 2 billion to be issued in 2018). There is also an annual deficit target for the general government budget of 1% of GDP in the medium term. The budget deficit could be lower than the target or fiscal surplus can be achieved in years when the GDP real growth is higher than the potential, while in years when the growth is lower than the potential, the deficit could be higher than the target. As to the more specific fiscal rules, salaries and pensions should remain frozen until their share in GDP falls below 7% for salaries and 11% for pensions. Except for the debt rule, there are no pre-defined consequences, in case of non-compliance, foreseen in the Budget System Law. Serbia acknowledged that since their introduction, Serbia has not complied with any of these numerical fiscal rules.

In addition to these rules, the Public Debt Law prescribes a limit on local government outstanding long-term borrowing for capital investment expenditures to 50% of the local government total revenues in the previous year. The amount of principal and interest due in any future year on all outstanding long-term borrowing for capital investments is limited as well to 15% of the total local government revenues in the previous year. Pursuant to Article 27h of the Budget System Law, the budget deficit of a local government in a given year cannot be greater than 10% of its revenues in that year. A deficit above this limit could be approved by the Ministry of Finance only if it is a result of the implementation of public investment. If a local government deficit exceeds the limit for a given year without the approval of the ministry, the minister could suspend the transfer of funds from the republican budget or the relevant part of the payroll tax and the corporate income tax in the next budget year for the amount exceeding the set limit.

According to Serbia, the Fiscal Council plays a significant consultative role in the budget process. It was established in accordance with Article 92 of the Budget System Law in 2010, as an independent body responsible for publicly overseeing fiscal sustainability and compliance with fiscal rules and reporting to the Assembly. The Fiscal Council has three members that are proposed by the President of Serbia, the Minister of Finance and the Governor of the NBS and appointed by the Assembly for a 6-year term (the term of the current members started in April 2011). The main duties of the Fiscal Council include preparing independent assessment of key policy documents (such as the Annual Budget Law and the Fiscal Strategy), assessing the fiscal effects of proposed laws, assessing government policy compliance with fiscal rules, and promoting reforms. It may also at any time, at its own initiative or upon request, provide advice to the Government on matters relating to fiscal policy and public finance management. Its freedom to communicate and access information are secured in law. The Council does not have executive authority but its reports and opinions have received wide publicity. By law, in case its recommendations on the Fiscal Strategy are not taken into account in the latter, a justification has to be published along with the document.

(i.4) *Medium-term budgetary frameworks*

The primary law that regulates the entire budget process at all levels of government is the Budget System Law. It determines the preparation, planning, adoption, execution, accounting and reporting of the budget. It defines, *inter alia*, the budget calendar, the fiscal rules, the content and adoption process of the Fiscal Strategy and the Fiscal Council jurisdiction and arrangement. The National Assembly also adopts annually the Law on the Budget.

The process of the preparation and adoption of the annual budget and financial plans of mandatory social security institutions should be carried out according to the budget calendar. It starts on 15 February with the issuance of an instruction by the Minister of Finance to propose the priority areas of financing for budgetary beneficiaries, including medium-term public investment priorities, and should end in mid-December with the National Assembly's adoption of the annual Law on the Budget and decisions on giving consent to financial plans of organisations for mandatory social security. Serbia acknowledged that in recent years, however, the difficult economic situation and budget underperformance triggered a number of budget revisions. According to the law, in the event that the National Assembly, and/or the local government assembly, does not adopt the budget within the time limits set out in the budget calendar, interim financing shall be performed during the maximum period of first three months of the fiscal year, with the possibility to be extended for three more months.

The medium-term fiscal and economic policy of Serbia is defined by the Fiscal Strategy. It covers the next year and the two subsequent years. By law, the Strategy should be adopted twice a year – in mid-June and a revised Strategy in the autumn. The Fiscal Strategy consists of three elements: macroeconomic and fiscal framework, public debt strategy and structural reforms. Serbia informed that in the last years the budget calendar could not be respected due to the difficult economic situation and the Strategy was adopted much later than the envisaged deadline. According to Serbia, the government submitted the Strategy to the National Assembly as prescribed by the Budget System Law but it has never been discussed.

(i.5) Transparency of general government finances and scope of budgetary frameworks

Serbia informed that reporting of main macroeconomic and budgetary aggregates is available monthly on a cash basis on the website of the Ministry of Finance. The budgetary aggregates are broken down at the level of subsectors (central government, health fund, pension fund, local governments, etc.) and consolidated for the general government. However, reports are preliminary and do not include data on own resources of some indirect budget beneficiaries and extra budgetary funds (except for Road Funds). Serbia declared that for every fiscal year the annual financial statement detailing budget execution, including indirect budgetary beneficiaries, is prepared and sent to the National Assembly in the form of a law, together with the decisions on annual financial statements of organisations for mandatory social security. Serbia acknowledged that in the last three years, the draft laws on the annual financial statement of the budget of the Republic of Serbia have not been discussed nor adopted by the National Assembly. In addition to the aforementioned reports, a consolidated budget report is adopted by the Government including all levels of government and indirect budget beneficiaries, but without extra budgetary funds.

(ii) Macroeconomic Imbalance Procedure

The Statistics Office of the Republic of Serbia in correspondence with the Ministry of Finance and the NBS collects a number of statistical indicators which are needed to participate in analyses conducted under the Macroeconomic Imbalance Procedure (MIP).

(iii) Structural reforms

The Economic Reform Programme 2015-2017 outlined key structural reform priorities. Serbia informed that the Government has established a Task Force, coordinated by the Ministry of Finance, with the support of the Public Policy Secretariat of the Republic of Serbia, in order

to improve the consistency of planned structural reforms with the overall fiscal and economic policy. According to Serbia, inter-ministerial coordination was improved in 2015 with the nomination of ERP coordinators in the relevant institutions and creation of the ERP network, ensuring broad ownership of the exercise.

III. ASSESSMENT OF THE DEGREE OF ALIGNMENT AND IMPLEMENTATION CAPACITY

This part summarises the Commission's assessment of the degree of alignment with the *acquis* in this field and Serbia's implementation capacity.

The legislation of Serbia is at a satisfactory level of alignment with the *acquis* on economic and monetary policy. Serbia possesses a good institutional and administrative framework in the field. However, its legislation on monetary policy and the functioning of the central bank need to be further aligned with the *acquis* in order to ensure the central bank's functional and institutional independence. In terms of economic policy, the budgetary framework is not yet in line with the *acquis* and improvements are needed to secure full transposition of Council Directive 2011/85 on requirements for national budgetary frameworks. Serbia will need to develop further its administrative capacity in order to participate in the fiscal and the broader economic and financial surveillance of the EU. Further efforts are needed to increase the capacity for economic planning, coordination and implementation. The structural reform framework is coherent and sufficiently comprehensive. However, the implementation record of the announced reforms needs to be improved.

III.a. Monetary policy

(i) Functional independence

Article 3 of the Law on the NBS identifies as the primary objective of the NBS the achievement and maintenance of price stability. This is compatible with Article 127 of the TFEU which stipulates that the primary objective shall be to maintain price stability. The NBS holds the full set of monetary policy instruments required for the steering of the money supply and therefore has all appropriate instruments to influence price stability.

The following provisions in the Serbian legislation, which are considered not fully compatible with the independence requirements, will need to be brought in line with the *acquis*:

- In order to ensure the functional independence of the NBS, the Law on the NBS should clearly and in a legally sound way state the objectives, other than the main objective, and define precisely the tasks and functions of the NBS, in line with Article 2 of the ESCB/ECB Statute.

- Article 3 of the Law on the NBS states that without prejudice to its previous objectives, the NBS shall support the pursuance of economic policy of the Government of the Republic of Serbia, operating in accordance with the principles of a market economy. By the time of accession of Serbia to the euro area, Article 3 of the Law on the NBS will need to be brought in line with Article 127(1) of the TFEU and Article 2 of the ESCB/ECB Statute, according to which the secondary objective of the NBS shall be to support the general economic policies of the Union.

(ii) Institutional independence

The Constitution of the Republic of Serbia stipulates that the NBS shall be autonomous and subject to oversight by the Assembly to which it shall also be accountable for its work. Article 2 of the Law on the NBS contains a general prohibition on giving/taking instructions and stipulates that the NBS, its bodies and the members of those bodies shall neither seek nor take instructions from government bodies and institutions, or other persons. It also stipulates that third parties, i.e. government bodies and institutions, and other persons may not threaten the autonomy and independence of the NBS nor seek to influence the NBS, its bodies, or the members of these bodies in carrying out their tasks. However, in order to achieve full compliance with the EU legislation, Serbia needs to pursue some legislative changes.

The following provisions in the Serbian legislation, which are considered not fully compatible with the independence requirements, need to be brought in line with the *acquis*:

- Article 2 of the Law on the NBS should be amended to explicitly state that the prohibition of seeking and taking instructions relates to institutions, bodies, offices and agencies of the EU as well and that these provisions are without prejudice to the powers of the ECB as stipulated in the ESCB/ECB Statute.

- Pursuant to the Constitution of the Republic of Serbia and Article 2 of the Law on the NBS, the NBS shall be subject to oversight by the National Assembly, to which it shall also be accountable for its work. In order to ensure full independence of its central bank, as prescribed by the TFEU and the ESCB/ECB Statute, Serbia will need to amend Article 2 of the Law on the NBS to ensure that this provision does not in any way allow the NBS to take instructions from the National Assembly, thus undermining its institutional independence.

- Pursuant to Article 10 of the Law on the NBS, the NBS cooperates with the Government and other state bodies in the performance of its tasks. Pursuant to Article 16, the Minister of Finance is regularly invited to participate in the meetings of the Executive Board without the right to vote. The cooperation between the NBS and the Government on exchange of information is regulated by non-binding agreements. The active participation of the Minister, even without voting right, to discussions where monetary policy is set could structurally offer the Government the possibility to influence the central bank when taking its key decisions. Therefore, Article 16 of the Law on the NBS will need to be amended so as to make sure that the attendance of members of the Government to NBS Executive Board meetings, even without voting rights, does not create a situation whereby the independence of the central bank could be weakened structurally. Although a representative of the Government can be invited to attend Executive Board meetings without voting rights, there should be no obligation to extend such invitation.

(iii) Personal independence

Articles 19 and 20 of the Law on the NBS comply with the general requirement under Article 14.2 of the ESCB/ECB Statute as regards the requirement of security of tenure for the term of office of a Governor.

Article 28 of the Law on the NBS is considered not fully compatible with the independence requirements and will need to be brought in line with the *acquis*:

- Article 14.2 of the ESCB/ECB Statute stipulates that national central bank Governors who have been dismissed from office may refer such a decision to the Court of Justice of the European Union. National legislation should either refer to the Statute or remain silent on the right to refer such a decision to the Court of Justice of the European Union (as Article 14.2 of the ESCB/ECB Statute is directly applicable). The Law on the NBS remains silent on this as it only refers to 'the Constitutional Court'. Serbia will need to amend its law with such proceedings thus bringing it in line with Article 14.2 of the ECB/ESCB Statute by the date of accession.

(iv) *Financial independence*

Pursuant to Article 81 of the Law on the NBS, the NBS selects an external auditor for a period of minimum three business years. The NBS is subject to the audit of the State Audit Institution but only in relation to public assets utilisation and transactions with the state budget. The audit should be performed on a non-political, independent and purely professional basis. The audit should comply with the prohibition of giving instructions to national central banks and their decision-making bodies and should not cover the NBS's ESCB-related tasks.

Pursuant to Article 79 of the Law on the NBS, the Council of the Governor shall submit the annual financial statements, along with the external auditor's report, to the National Assembly, for information purposes. In order to protect the financial and institutional independence of the NBS, it should be ensured that the submission of the financial statements and the auditor's report is only for information purposes and does not involve consultations with the National Assembly.

The following provisions in the Serbian legislation, which are considered not fully compatible with the independence requirements, will need to be brought in line with the *acquis*:

- As regards property rights, the NBS uses public property without an obligation to pay rent. Pursuant to Article 27 of the Law on Public Property, the Government decides on the alienation of NBS's immovable and on establishing a mortgage on them. This article will need to be amended to allow the NBS to dispose of its property independently.

(v) *The prohibition of monetary financing*

Article 62 of the Law on the NBS contains a provision prohibiting the monetary financing of the public sector, corresponding to Article 123 of the TFEU. Nevertheless, the range of public sector entities referred to in this paragraph needs to be extended to be completely consistent with the Treaty. Article 62 covers the public administration, central, regional and local public authorities and legal persons. To achieve full harmonisation with Article 123 of the TFEU, the definition in Article 62 will need to be extended to cover central, regional, local and other public authorities, other bodies governed by public law and public undertakings of the other Member States and Union institutions and bodies.

Article 38 of the Law on the NBS authorises the NBS to grant short-term emergency liquidity assistance (ELA) to a solvent bank against adequate collateral instruments in exceptional circumstances. Further details are provided in the Decision on terms and conditions of extending liquidity loans to banks. The instrument created by the above-mentioned provision of the Law on the NBS complies with the requirements of Article 123 of the TFEU.

(vi) The prohibition of privileged access of public authorities to financial institutions

The Law on Banks does not contain provisions that can be regarded as establishing privileged access to financial institutions as defined by Article 124 of the TFEU, and is therefore in line with the *acquis*.

(vii) The integration of the central bank into the ESCB

Serbia will need to complement its Law on the NBS with the necessary provisions ensuring the integration of the NBS into the ESCB from the date of adoption of the euro. This includes provisions ensuring its subordination to the guidelines and instructions of the ESCB and ECB as from the date of the formal adoption of the euro.

III.b. Economic policy

In the field of economic policy, Serbia will need to participate in the coordination of economic policies at the EU level. According to Article 121 of the TFEU, Member States shall regard their economic policies as a matter of common concern and shall coordinate them within the Council. The European Semester is the EU's annual cycle of economic policy guidance and surveillance. Under the Stability and Growth Pact and the Macroeconomic Imbalance Procedure, which concern all Member States, the aim is to identify potential risks, prevent or correct excessive fiscal deficits and harmful macroeconomic imbalances and correct the imbalances that are already in place. Member States are also required to submit National Reform Programmes (NRP) outlining medium-term structural reform plans.

Serbia already participates in pre-accession economic surveillance since 2006, when it submitted its first Economic and Fiscal Programme. In 2012, when Serbia was granted candidate status, it submitted its first Pre-accession Economic Programme. The last Pre-accession Economic Programme was submitted in January 2014. From 2015 onwards, Serbia now submits an Economic Reform Programme. The ERP contains both a macro-fiscal framework (similar to the Stability or Convergence Programmes submitted by Member States under the Stability and Growth Pact) and structural reform plans (similar to the NRPs). This contributes to developing the administrative capacity of the country for future participation in economic and fiscal policy coordination as well as broader economic and financial surveillance.

(i) Budgetary surveillance

By the time of accession, Serbia will need to avoid excessive government deficits in accordance with article 126 of the TFEU and Regulations 1466/97 and 1467/97. The respective reference values determined in Protocol 12 to the TFEU are 3% for the ratio of the government deficit to gross domestic product at market prices and 60% for the ratio of government debt to GDP, unless the debt is sufficiently diminishing and approaching the reference value at a satisfactory pace.

By the time of accession, Serbia will also need to define a medium-term budgetary objective (MTO), set in structural terms which will reflect the need to ensure the sustainability of the public finance over time. The value of the MTO set by Serbia should be at least equal to the minimum value of the MTO calculated by the European Commission. With its MTO defined, Serbia will need to keep its structural balance at or above its MTO, or be on an appropriate

adjustment path towards it. The adjustment path will have to be assessed by looking at both the evolution of the structural balance and the dynamics of expenditure net of discretionary revenue measures. The adjustment path should be in line with the requirements of the Stability and Growth Pact. Although Serbia's ERP and Fiscal Strategy include calculations of the structural balance, further improvements in forecasting, simulating tools and analytical capacities are needed in order to effectively participate in the European Semester.

Serbia will need to make further efforts to align its legislation with the *acquis* in the field of economic policy. Serbia has to align its budget legislation and practices with the requirements set in Directive 2011/85, outlined below.

(i.1) *Accounting and statistics*

In the area of accounting and statistics, Member States are required to have a public accounting system in place that generates accrual data with a view to preparing fiscal data based on ESA 2010 standard, in accordance with Directive 2011/85 on requirements for budgetary frameworks of the Member States. Member States shall also ensure timely and regular public availability of fiscal data for all sub-sectors of general government.

Serbia publishes detailed and regular reporting on a monthly basis. However, there is a need to better define the scope of general government by expanding it to include all relevant entities and to streamline the existing definitions and statistics of government debt. While national account statistics underpin policy design and coordination activities, the quality of input statistics will need to be ensured in line with Regulation 549/2013 (see Chapter 18: Statistics).

(i.2) *Macroeconomic and budgetary forecasts*

Directive 2011/85 also requires Member States to ensure that fiscal planning is based on realistic macroeconomic and budgetary forecasts that include a sensitivity analysis. The Ministry of Finance of Serbia produces both macroeconomic and fiscal forecasts and is already engaged in a technical dialogue with the Commission concerning the assumptions underpinning their preparation. However, further efforts are needed to enhance the analytical capacity for macro-fiscal projections. In particular, Serbia will need to strengthen its expertise and human resources for macroeconomic and budgetary forecasting and analysis and for dissemination of main fiscal data and underlying assumptions. The methodologies, assumptions and relevant parameters on which such forecasts are based will need to be made publicly available and macroeconomic and budgetary forecasts compared with the most updated forecasts of the European Commission. The macroeconomic and budgetary forecasts for fiscal planning will need to be subject to regular, unbiased and comprehensive evaluation based on objective criteria, including *ex post* evaluation. The result of evaluations will need to be made public and taken into account appropriately in future macroeconomic and budgetary forecasts.

(i.3) *Numerical fiscal rules*

Serbia has set national numerical fiscal rules as required by Directive 2011/85. However, their relevance to effectively guide budget planning and execution in accordance with the EU fiscal framework will have to be reviewed. In line with Directive 2011/85, Serbia will need to pre-define consequences in the event of non-compliance with its fiscal rules. This is all the more

important considering that up until now the numerical fiscal targets have not been attained. The established monitoring role of the Fiscal Council is an asset.

(i.4) Medium-term budgetary frameworks

Member States shall establish a credible, effective medium-term budgetary framework with a planning horizon of at least three years in accordance with Directive 2011/85. Serbia has a multi-annual budgetary framework in place in the form of the Budget System Law, which governs the Fiscal Strategy. The Fiscal Strategy includes multiannual budgetary objectives in terms of the general government deficit and debt and projections of major expenditure and revenue items of the general government. It also outlines the envisaged medium-term policies with an impact on general government finance, broken down by major expenditure and revenue item. The Strategy presents as well the expected developments of government debt over the long-term, until it reaches the target, established by fiscal rules.

The Fiscal Strategy is the basis for the Government's Economic Reform Programme. The ERP 2015-17 presented a clear and concise picture of past developments and a sufficiently comprehensive and coherent macroeconomic framework. The macroeconomic scenario was plausible and major uncertainties and risks were outlined. The fiscal framework was consistent and integrated with the overall policy objectives.

However, the Budget System Law will need to be further improved and rigorously implemented. Budget calendars have to be followed and the statistical coverage and definition of the general government sector improved. Programme budgeting has to be strengthened, and administrative and IT capacities reinforced, so as to allow for a better policy making, budget preparation and implementation over the medium term. In addition, an assessment of the direct impact of envisaged policies on the long term sustainability of public finances will have to be developed.

(i.5) Transparency of general government finances and scope of budgetary frameworks

Further efforts will be needed to ensure that fiscal planning, fiscal rules and forecasts are comprehensive in coverage across sub-sectors of general government as required by Directive 2011/85.

A basic condition for participating in the EU economic and fiscal surveillance is the timely provision of quality fiscal and economic data in accordance with Regulation 479/2009. Therefore, Serbia should start submitting official fiscal notifications as soon as possible, and continue doing so on a regular basis in order to be able to provide fiscal data of sufficient standard and quality already in the pre-accession period (See also Chapter 18: Statistics).

There is also a need to improve monitoring of arrears, budgetary commitments, and develop systems and registers used in the budgetary process. As required by Directive 2011/85, Serbia will need to publish relevant information on contingent liabilities with potentially large impact on public finances, including government guarantees, non-performing loans, and liabilities stemming from the operation of public corporations. Serbia will need to publish information on the participation of general government in the capital of private and public corporations in respect of economically significant amounts. The national Assembly will need to better engage in the monitoring process, in line with the current national legislation.

(ii) Macroeconomic Imbalance Procedure

By the time of accession, Serbia will need to participate in the Macroeconomic Imbalance Procedure in accordance with Regulation 1176/2011. In this context, Serbia will have to collect the necessary statistics in order to contribute to the scoreboard, currently consisting of a set of 14 indicators covering the major sources of macroeconomic imbalances. The scoreboard includes indicators related to the current account balance and the international investment position, unit labour costs, unemployment, house prices and private sector debt among others. Although currently Serbia shares some of these indicators with the Commission in the context of the Economic Reform Programme and in the sub-committee on economic and financial matters, indicating Serbia's readiness to participate in the MIP, further efforts will be needed to secure the timeliness and quality of all relevant data under the procedure.

(iii) Structural reforms

In accordance with the Council Recommendation on the Broad Economic Policy Guidelines, Member States submit National Reform Programmes (NRP) outlining structural reform plans aimed at supporting the goals of the Europe 2020 Strategy. Serbia's Economic Reform Programme 2015-2017 consisted of comprehensive macroeconomic, fiscal and structural reform parts. However, the programme did not provide information on the budgetary implications of some of the major structural reforms. In addition, the link between priority measures for sectoral reforms and broader policy objectives remains weak. These weaknesses highlight a need to strengthen inter-ministerial policy coordination in order to improve national economic policy effectiveness.
