

SERBIA: PUBLIC FINANCE – TOWARD THE EFFICIENT MANAGEMENT OF THE COUNTRY’S REVENUES



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Abstract

Like other countries of South-East Europe, the Republic of Serbia aims to join the European Union (EU). Within the Stabilisation and Association Process, Serbia has undertaken steps to harmonise its national legal system with that of the EU, as well as actions that seek to establish a functional market economy. However, Serbia's present geopolitical position outside of the EU allows for a larger autonomy in conducting its national economic policy. This chapter examines the particularities of the elaboration and enforcement of fiscal policy, and more specifically public finance, from the perspective of an EU candidate country. The Serbian public finance system is not fully aligned with EU law; however, the reforms implemented thus far were considered sufficient for opening the EU-Serbia negotiation chapters (now, clusters) pertaining to the area of public finance. Under the general fiscal rules prescribed by the Budget System Act, the government sector debt, including the liabilities based on restitution, should not exceed 60% of gross domestic product (GDP), while the target medium-term fiscal deficit should represent 0.5% of the GDP. Under the principles of responsible fiscal management, the employee expenses in the government sector must be fixed at a sustainable level; thus, efforts are made to keep the proportion of these expenses in the GDP under 10%. Although the budgetary procedure is well designed, the 'regular' path for budget adoption was not always observed in the past, mainly due to economic perturbations caused by the COVID-19 pandemic.

Keywords: *public finance, Serbia, budget, European integrations, Fiscal Council*

Dušan V. Popović (2024) 'Serbia: Public Finance – Toward the Efficient Management of the Country's Revenues'. In: Zoltán Nagy (ed.) *Economic Governance. The Impact of the European Union on the Regulation of Fiscal and Monetary Policy in Central European Countries*, pp. 167–180. Miskolc–Budapest, Central European Academic Publishing.

https://doi.org/10.54237/profnet.2024.znecogov_7

1. Introduction

Like other countries of South-Eastern Europe (hereinafter: the ‘SEE countries’), the Republic of Serbia aims to join the European Union (EU). In 1993, the European Council in Copenhagen defined the accession criteria (also known as the ‘Copenhagen criteria’), which represent the essential conditions all candidate countries must satisfy to become an EU Member State. Further to reaching adequate political stability and institutional capacity, each EU candidate country must establish a functioning market economy and the capacity to cope with competition and market forces. Following the pre-accession experience of Central and Eastern European countries that joined the EU in 2004 and 2007, the EU defined the Stabilisation and Association Process. This process is an enlargement policy based on the Stabilisation and Association Agreements (SAAs) each SEE country has concluded with the Union.

The SAAs are modelled on the Europe agreements that the EU signed with Central and Eastern European countries in the 1990s. These SAAs are international agreements concluded with the objective of preparing the candidate or potential candidate country for EU membership. Each SAA clearly defines the aims of the association; for example, the SAA concluded with the Republic of Serbia indicates the following aims: (i) supporting Serbia’s efforts to strengthen democracy and the rule of law; (ii) contributing to political, economic, and institutional stability in Serbia, as well as to the stabilisation of the region; (iii) providing an appropriate framework for political dialogue to allow for the development of close political relations between the parties; (iv) supporting Serbia’s efforts to develop its economic and international cooperation, including the approximation of its legislation to that of the European Community; (v) supporting Serbia’s efforts to complete the transition into a functioning market economy; (vi) promoting harmonious economic relations and gradually developing a free trade area between the European Community and Serbia; and (vii) fostering regional cooperation in all the fields covered by the SAA.¹ The necessity of a framework for political cooperation and regional dialogue is highlighted. This goes together with the obligation to commit to economic cooperation and development. The concept of four freedoms (i.e. the free movement of workers, capital, goods, and services) and the principle of free competition, both included in the EU’s internal market, are extended to these association agreements. The SAAs also provide for asymmetric trade liberalisation between the EU and each of the SEE countries. The approximation of laws consists of the adoption of the EU *acquis* in the respective countries’ legal systems. The SAAs set a timeframe for the approximation efforts undertaken by the corresponding SEE country. The SEE countries have all reached different stages in the European integration process. Serbia signed the SAA in 2008 and was granted EU candidate status in 2012.

1 Stabilisation and Association Agreement between the European Communities and their Member States of the one part, and the Republic of Serbia of the other part, Art. 1 para. 2.

With respect to economic and trade policy, the SAA concluded between the EU and the Republic of Serbia envisages that the two parties shall cooperate to (i) exchange information on macroeconomic performance and prospects and on strategies for development; (ii) jointly analyse economic issues of mutual interest, including the framing of economic policy and the instruments for implementing it; and (iii) promote wider cooperation with the aim of speeding up the inflow of know-how and access to new technologies. Further to this, Serbia is required to establish a functioning market economy and gradually approximate its policies to the stability-oriented policies of the European Economic and Monetary Union.² Serbia's present geopolitical position of Serbia outside of the European Union allows for greater autonomy in conducting its national economic policy and, to a certain extent, its public finance.

The efficient and transparent management of public finances increases the trust in state institutions and benefits citizens through better healthcare, social, and other public services, as well as a higher standard of living.³ Moreover, healthy public finances contribute to companies becoming more competitive in the market and economic growth. Improved public financial management is a necessary step on Serbia's path to joining the EU. The budget of the Republic of Serbia and some other countries in the region of former Yugoslavia accounts for a significant part of the national gross domestic product (GDP). As such, public financial management is essential for economic development, the availability of public services, and citizens' quality of life. Relations between the central government and local authorities, as well as decentralisation and transparency in the spending of public funds, are equally important areas of public finance. To improve the performance of its public finance sector, the Republic of Serbia joined the UN 2030 Agenda. The Sustainable Development Goals of the 2030 Agenda formally came into effect on 1 January 2016, following the adoption of a resolution at the UN summit in September 2015. Up until 2030, the signatories are expected to mobilise all resources to eradicate poverty, fight inequality, and devise a response to climate change. The Sustainable Development Goals, which build on the Millennium Development Goals and recognise that the fight against poverty goes hand in hand with economic growth and industrialisation, are geared toward several societal needs, including health, education, social protection, a healthy environment, and communities resilient to climate change.⁴ This means that all development plans and policy documents in the process of Republic of Serbia's EU integration also integrate the 2030 Agenda and use it to profile the Republic of Serbia as a future EU Member State.

In this chapter, the system of public finances in the Republic of Serbia is presented through an analysis of the budgetary procedure, budget constraints, and the

² SAA, Art. 89.

³ For alternative definitions, see: Kennedy, 2012, pp. 3–4; Tanzi, 2020, pp. 11–29; Rosen, 2008, p. 371.

⁴ For an in-depth analysis of Serbia's implementation of the 2030 Agenda objectives, see: Government of the Republic of Serbia, Public Policy Secretariat, 2022.

role and responsibilities of the Fiscal Council, as well as an overview of the main characteristics of the ongoing Public Finance Management Reform Programme.

2. Budgetary procedure

The Budget System Act (BSA)⁵ is the main legislative instrument regulating the planning, preparation, adoption, and execution of the budget of the Republic of Serbia and those of autonomous provinces (Vojvodina, and Kosovo and Metohija) and local self-governments. The BSA also regulates the preparation and adoption of the financial plans of organisations related to mandatory social insurance, which include (i) the Republic Fund for Pension and Disability Insurance, (ii) the Republic Fund for Health Insurance, (iii) the Military Social Security Fund, and (iv) the National Employment Service. Similarly to other jurisdictions, the Serbian BSA specifies what budgetary processes are prescribed in law, who is responsible, and when key budgetary steps should be taken.

The question of how budget processes are implemented is also regulated to a certain extent by the BSA, although by-laws are more appropriate for this purpose in many cases. The BSA prescribes that the budget system should achieve the following goals: (i) overall fiscal sustainability and control, which implies the implementation of policies without significant changes in the consolidated general government, with comprehensive control of total budget funds, through the establishment of expenditure and outflow ceilings that are guaranteed by the law, at both the overall and budget beneficiary levels; (ii) allocation efficiency, which implies a possibility of setting priorities within the budget, allocating funds in line with the government priorities within the budget, and transferring funds from old to new or less productive to more productive priorities; (iii) technical or operational efficiency, which implies the use of budget funds and the possibility of their application with the lowest possible costs; and (iv) allocation efficiency, which implies allocating budget funds in order to promote gender equality.⁶

The BSA recognises the following types of public revenues: (i) taxes; (ii) contributions for mandatory social insurance; (iii) non-tax revenues, namely, fees, charges, fines, and other non-tax revenues; (iv) self-contribution; and (v) grants, transfers, and financial assistance from the EU.⁷ The BSA also lays down a closed list of types of government proceeds: (i) proceeds from the sale of non-financial assets, (ii) proceeds from

5 Budget System Act, *Official Journal of the Republic of Serbia* 54/2009, 73/2010, 101/2010, 101/2011, 93/2012, 62/2013, 63/2013, 108/2013, 142/2014, 68/2015, 103/2015, 99/2016, 113/2017, 95/2018, 31/2019, 72/2019, 149/2020, 118/2021, 138/2022 and 118/2021, Art. 1.

6 BSA, Art. 4.

7 See also: Popović, 2022, pp. 3–15.

borrowing, and (iii) proceeds from the sale of financial assets.⁸ In addition to types of public revenues and proceeds, the BSA enumerates several types of government public expenditures and outflows. The public expenditures recognised by the BSA include (i) expenditures for employees, (ii) expenditures for goods and services, (iii) amortisation and usage of equipment, (iv) payment of interest and borrowing-related expenses, (v) subsidies, (vi) financial assistance and transfers, (vii) mandatory social insurance and social security, and (viii) other expenditures. The BSA enlists the following government outflows: (i) outflows for the acquisition of non-financial assets, (ii) outflows for principal repayment, and (iii) outflows for the acquisition of financial assets.⁹

The budget of the Republic of Serbia is adopted by the National Assembly. The government is responsible for the execution of this budget, which is prepared and adopted in accordance with the budget calendar prescribed by the BSA. Namely, on 15 February, the Minister of Finance provides instructions for proposing priority areas of financing for the budget beneficiaries. On 15 March, based on the instructions received from the Minister of Finance, the direct beneficiaries of the budget are required to provide proposals for determining the priority areas of financing for the budget year, as well as for the two following fiscal years, to the Ministry of Finance. By 15 May, the Minister of Finance must prepare the Draft Fiscal Strategy, which lays out the government's economic and fiscal policies. This strategy includes projections for the budget year and the two following fiscal years, specific decisions on priority areas for financing, and the medium-term priorities for public investment. By 1 June, the Fiscal Council must provide an opinion on the Draft Fiscal Strategy. Thereafter, by 5 June, the Minister of Finance is required to provide the government with a proposal of the Fiscal Strategy for adoption. The government is expected to adopt the Fiscal Strategy by 15 June and submit it to the Financial Committee of the National Assembly for consideration. On 5 July, the Minister of Finance shall provide instructions for the preparation of the draft budget. Then, on 15 October, the government is required to adopt the revised Fiscal Strategy, inclusive of the information on the financial and other effects of the new policies, taking into account the macroeconomic framework updated after 15 May. On 20 October, the government should provide the revised Fiscal Strategy to the Financial Committee of the National Assembly. Finally, on 1 November, the Minister of Finance provides the government with the Draft Act on the Budget, which the government adopts by 15 November, thereafter submitting the proposal to the National Assembly. On 20 December, the National Assembly is scheduled to pass the Budget Act of the Republic of Serbia.¹⁰

Once adopted, the BSA and the revised Fiscal Strategy are published in the Official Journal of the Republic of Serbia. The budget is adopted for the period of one fiscal year and is effective for the year for which it was adopted. The fiscal year is a 12-month period, commencing on 1 January and ending on 31 December of each

⁸ BSA, Art. 14.

⁹ BSA, Art. 27.

¹⁰ BSA, Art. 31.

calendar year. The budget may also be adopted for the period of three fiscal years. In the event that the National Assembly does not adopt the budget within the time limits set out in the budget calendar, interim financing shall be conducted for a maximum period of the first three months of the fiscal year.¹¹ The interim financing period may be extended for three additional months, thus lasting for a total period six months, in the event that the budget is not adopted before 15 March of the current budget year.

Further to regulating the central budget (the Budget of the Republic of Serbia), the BSA lays out specific rules on the planning, preparation, adoption, and execution of the budgets of autonomous provinces, cities, and municipalities. The regional and local budgets are adopted in accordance with a somewhat different budget calendar. By 1 August, the local government finance authority is required to provide instructions for the preparation of the draft local government budget. By 15 September, the direct beneficiaries of the local government budget must provide the draft financial plan to the local government finance authority for the budget year and two following fiscal years, which should include a performance report for the programme for the first six months of the current year. By 1 November, the local government finance authority is required to provide a draft decision on the budget to the competent executive authority of the local government. Thereafter, by 15 November, the competent executive authority of the local government should provide a proposed decision on the budget to the local government assembly. By 20 December, the local government assembly¹² is required to pass the decision on the local government budget. Finally, by 25 December, the local government finance authority is bound to deliver the decision on the local government budget to the Minister of Finance.¹³

3. Budget constraints

The BSA sets out several principles of responsible fiscal management that must be observed by both central and local governments and budget beneficiaries. The general fiscal principles are (i) the principle of accountability, (ii) the principle of fairness, (iii) the principle of responsibility, (iv) the principle of stability, and (v) the principle of transparency.¹⁴ The principle of accountability means that the central, regional, or local government is accountable to the assembly for the execution of its responsibilities in relation to the management of fiscal policy. The principle of fairness means that the management of fiscal policy is implemented in such a manner as to

¹¹ BSA, Art. 46.

¹² Assembly of an autonomous province, city assembly, or municipal assembly.

¹³ BSA, Art. 31. For a more detailed analysis of local budgetary procedure and principles see: Raičević et al., 2003, pp. 175–191.

¹⁴ BSA, Art. 27b.

take into account its impact on the well-being of present and future generations. The principle of responsibility comprises managing public assets and liabilities, natural resources, and fiscal risks in such a way as to reinforce fiscal sustainability. The principle of stability means that fiscal policy is implemented in a way that prevents sudden changes in trends of macroeconomic and fiscal indicators. Finally, the principle of transparency implies the clear identification and definition of the tasks and responsibilities of the various government authorities and/or local government bodies and officials in relation to the management of fiscal policy.¹⁵ Further to these general fiscal principles, the BSA sets out the specific principles according to which the government should determine and implement the objectives of the fiscal policy, as follows: (i) the sustainability of state debt; (ii) the regular servicing of debt; (iii) the predictability of tax rates and the tax base for the following year; (iv) the responsible management of fiscal risks; (v) the management of public assets, public liabilities, and natural resources in a manner that does not burden future generations; and (vi) the promotion of economic growth.¹⁶

Under the general fiscal rules prescribed by the BSA, the government sector debt, including liabilities based on restitution, should not exceed 60% of the country's GDP, whereas the target medium-term fiscal deficit should represent no more than 0.5% of GDP. If the government sector debt is higher than 60% of GDP, the fiscal position of the government sector must be balanced so that the fiscal deficit is 0% of GDP at maximum. If the government sector debt is between 55% and 60% of GDP, the fiscal deficit should be 0.5% of GDP at the maximum. If the government sector debt is between 45% and 55% of GDP, the fiscal deficit should be 1.5% of GDP at maximum. Further, if the government sector debt is below 45% of GDP, the fiscal deficit should not exceed the amount of 3% of GDP. If the fiscal deficit laid down by the general fiscal rule prescribed by the BSA is exceeded, the government shall, at the proposal of the Ministry of Finance, pass a decision on a programme of measures to adjust the excessive fiscal deficit in the medium-term. Upon obtaining a reasoned opinion of the Fiscal Council, the government must provide this programme to the National Assembly for informational purposes. If the government sector debt exceeds or is predicted to exceed 55% of GDP, the government must submit to the National Assembly, together with the budget for the following year in the Fiscal Strategy, as well as in the revised Fiscal Strategy, a programme to reduce government sector debt relative to GDP. The government must also submit a report on the implementation of the debt reduction programme and the updated programme for each subsequent year in which this debt remains above 55% of GDP. Finally, if the government sector debt exceeds or is predicted to exceed 60% of GDP, the National Assembly shall adopt the

15 In public finance theory, budget transparency may have a two-fold meaning. First, transparency may refer to the outputs of budgeting; here the ideal is that the tradeoffs inherent in a budget should be made clear and understandable to policy-makers and the public. Second, transparency may refer to the inputs of budgeting; here, the ideal is to ensure that the decision-making process is itself conducted in public. See: Garrett and Vermeule, 2006, pp. 2–3.

16 BSA, Art. 27b.

debt reduction programme once a year at minimum in the course of the preparation and adoption of the budget for the following fiscal year.¹⁷

The general government debt-to-GDP ratio fell from a peak of over 70% in 2015 to 53% in 2019. It then increased to 57.8% in 2020 as a result of the high crisis-induced deficit, before broadly stabilising at 57.1% in 2021 and 55.10% in 2022.

The BSA also prescribes special fiscal rules with the objective of ensuring that the target fiscal deficit and government sector debt-to-GDP ratio are achieved through restrictions on public expenditures. Under the principles of responsible fiscal management, employee expenses in the government sector must be fixed at a sustainable level, with efforts made to keep the share of these employee expenses in the GDP under 10%. Further to this, salaries and/or wages can only be raised in a year in which, based on the relevant planning documents of the competent authorities, the share of employee expenses in the government sector within the GDP is expected and/or assessed to be up to 10%, and only in such a manner that this expected share is kept under the stipulated percentage following the adjustment.¹⁸ Moreover, the BSA establishes rules on the fiscal deficit of local authorities, which may not exceed 10% of their revenues in a given year. The local government may submit a request for the approval of a fiscal deficit above the specified level to the Ministry of Finance only in cases in which such a deficit is the result of implementing public investments.¹⁹

In the event of natural disasters and external shocks that may endanger human health and national security and provoke a significant decline in economic activity, the government may temporarily deviate from the fiscal principles and rules. A decision regarding such a deviation must be submitted to the National Assembly for informational purposes. This decision must indicate the reasons for the deviation from the rules, the measures that the government intends to take to re-comply with the fiscal rules, and the timeframe for re-compliance with the rules. It must also present medium-term fiscal plans demonstrating the level of fiscal deficit and debt of the state and the public sector.²⁰

4. The Fiscal Council

In October 2010, significant amendments to the BSA resulted in the introduction of fiscal rules as a foundation of a responsible fiscal policy and the establishment of a Fiscal Council as an independent state body accountable to the National Assembly. The Fiscal Council was formed with the objective of improving the culture

17 BSA, Art. 27e.

18 BSA, Art. 27e.

19 BSA, Art. 27ž.

20 BSA, Art. 27z.

of fiscal responsibility in the Republic of Serbia through the provision of independent analyses of fiscal policy and encouraging professional debate on fiscal policy. The Fiscal Council's mission is to assess the credibility of the fiscal policy in terms of compliance with established fiscal rules and to provide publicity and ensure responsibility in the implementation of this policy. The Council reviews the macroeconomic and fiscal suppositions underpinning the development of government documents, provides an independent and credible assessment of the economic policy, assesses fiscal risks and the prospects for the government to fulfil its fiscal objectives in the future, and evaluates to what extent the government has respected fiscal rules in the past.

Three types of fiscal councils can be differentiated in legal and economic theory: 'soft' councils, 'hard' councils, and 'very soft' councils.²¹ The first type of council has only an advisory role and publishes its recommendations. The second type is empowered to adopt binding decisions on the budget. Finally, the third type is formed by experts from academia, and its decisions are available only internally to state institutions.²² The Fiscal Council of the Republic of Serbia largely corresponds to the first, 'soft' type of council. The International Monetary Fund has argued in favour of strengthening national fiscal councils and aligning their status in terms of institutional capacity, proficiency, experience, operational independence, and key functions such as mandates, tasks, and access to information.²³

The Fiscal Council of the Republic of Serbia consists of three members appointed by the National Assembly. One member is nominated by the President of the Republic, another by the Minister of Finance, and the third by the Governor of the National Bank of Serbia.²⁴ Members of the Fiscal Council must be citizens of the Republic of Serbia who do not perform another public function, have not been convicted, have at least five years of work experience, hold a postgraduate degree in the field of economics, and have published scientific papers on macroeconomics, fiscal policy, public finance, accounting, or other related scientific fields. In addition, a candidate for the presidency of the Fiscal Council must have at least five years of experience in performing managerial tasks. Members of the Fiscal Council must not be members of a political party nor be guided in their work by political beliefs.²⁵ Fiscal Council members are appointed for a term of six years; this term was chosen in order to avoid overlap with the four-year term for members of the National Assembly. The first three members of the Fiscal Council were appointed in March 2011, and the body became fully operational in April 2011.

Further to its general duty of assessing the credibility of the government's measures of economic policy, the Fiscal Council is empowered to perform the

21 See, for example: Calmfors and Wren-Lewis, 2011, pp. 11–12; Beetsma et al., 2018, pp. 3–4.

22 Anđelković, 2018, pp. 374–377.

23 Arnold et al., 2022, pp. 18–19.

24 BSA, Art. 92b.

25 BSA, Art. 92v.

following additional tasks: (i) prepare an opinion on the Draft Fiscal Strategy, (ii) prepare and submit an analysis of the revised Fiscal Strategy for the corresponding fiscal year and of the Draft Budget Act of the Republic of Serbia to the National Assembly, and (iii) prepare and submit estimates of fiscal impact of other laws and amendments that were submitted during the Assembly debate to the National Assembly.²⁶ The Fiscal Council may, at any time and on its own initiative, or upon request, provide advice to the government on issues related to fiscal policy and public finance management. For transparency reasons, and in order to raise awareness of responsible fiscal policy, all analyses, reports, recommendations, and advice prepared by the Fiscal Council are made publicly available within five working days from the date of their submission to the Minister of Finance, the government, or the National Assembly.

Although the BSA prescribes the Fiscal Council's participation in different stages of the budgetary procedure, there are no consequences for the government for not following the Council's recommendations. For example, if any of the Fiscal Council's recommendations are not included in the Fiscal Strategy, this must be stated, the reasons for this decision must be provided, and the delivered opinion of the Fiscal Council must be attached to the Fiscal Strategy in its entirety.²⁷ However, on several occasions, the Fiscal Council has complained that the government ignored its recommendations and did not provide any explanation for not taking them into consideration. For instance, in its opinion on the Draft Fiscal Strategy for 2022, dated June 2021, which included forecasts for 2023 and 2024, the Fiscal Council presented several recommendations aimed at improving the document's credibility (e.g. the recommendation to present the sectoral structure of subsidies, including those stemming from local government). According to the Fiscal Council, some of its recommendations were not included in the revised Fiscal Strategy and some were not adopted appropriately.²⁸

To properly discharge its duties and responsibilities, the Fiscal Council needs to obtain access to information; thus, the BSA empowers it to request that any government minister submit appropriate economic and fiscal forecasts and analyses. Furthermore, the Fiscal Council may require the Minister of Finance to prepare and submit fiscal projections based on alternative assumptions and scenarios. The Fiscal Council is also empowered to request information from any entity in the public sector, including public enterprises, if such information is essential to its work.²⁹ However, failure to comply with a request made by the Fiscal Council does not result in real sanctions as the BSA prescribes that the president of the Fiscal Council may only inform the National Assembly of any lack of cooperation by a public sector entity or governmental body.

26 BSA, Art. 92ž.

27 BSA, Art. 27g para. 3.

28 Republic of Serbia, Fiscal Council, 2021, pp. 2–3.

29 BSA, Art. 92i.

5. Public Finance Management Reform Programme

In November 2015, the government of the Republic of Serbia adopted the Public Financial Management Reform Programme 2016–2020³⁰ (hereinafter: the 'PFMRP 2016–2020'). The overall objective of the PFMRP 2016–2020 was to achieve a sustainable budget with a reduced debt-to-GDP ratio through stronger financial management and control and to improve the audit control process.³¹ The PFMRP 2016–2020 contained 19 different measures, including improving the credibility of macroeconomic forecasts, budget planning, and the coverage and reporting on budget execution; the further implementation of multi-year programme budgeting at all levels of government; improving the strategic and legislative framework for implementing internal financial control in the public sector; and enhancing regulations and procedures for public procurement. Multi-year programme budgeting was also introduced in 2015 for all budget users. The biggest improvement in the area of the financial control of public funds was achieved in May 2017 through the adoption of the Strategy of Public Internal Financial Control (PIFC) Development for the period 2017–2020.³² The implementation of the PIFC legislation and its underlying framework, as well as the development of sufficient administrative capacity at the central and local levels, in social security funds, and in state-owned companies, is one of the requirements for the temporary closure of the EU-Serbia negotiations on Chapter 32, which is dedicated to financial control. Under the new enlargement methodology, Chapter 32 is now part of Cluster 1 – Fundamentals, which illustrates the importance the EU attaches to developing financial control instruments.³³

In June 2021, the government of the Republic of Serbia adopted the Public Financial Management Reform Programme for the period 2021–2025³⁴ (hereinafter: the 'PFMRP 2021–2025'). The goal of the PFMRP 2021–2025 is to achieve a sustainable budget with stable public debt relative to GDP through better financial management and control, the internal audit process, and linking budget planning to government policies. Two of the key objectives of the PFMRP 2021–2025 are improving budget discipline and achieving the more transparent use of public funds. The roles involved in implementing the framework of internal control are divided between several entities. The Central Harmonisation Unit of the Ministry of Finance is tasked with designing, co-ordinating, and monitoring the frameworks of PIFC. The

30 Republic of Serbia, Ministry of Finance, 2015.

31 Apart from regular budget financing, the implementation of the programme was supported by the European Commission (IPA, TAIE), the GIZ project for public financial reform, the World Bank, the IMF, the OECD, and the UNDP.

32 Republic of Serbia, Ministry of Finance, 2016.

33 In March 2020, the EU revised its enlargement methodology for the Western Balkans. The main novelty in this enlargement methodology is the establishment of six negotiation clusters that cover several negotiation chapters.

34 *Public Financial Management Reform Programme 2021–2025* [Online]. Available at: https://www.mfin.gov.rs/upload/media/s47t6d_62612f05e7604.pdf (Accessed: 11 September 2023).

functioning of the established systems for management, risk monitoring, and the application of PIFC rules is subject to review by an independent, internal audit of the beneficiaries of public funds. The ex-post control of the compliance of financial transactions and operations of public-fund beneficiaries are entrusted to the Budget Inspection. Meanwhile, the roles of financial management, control, irregularity management, combating fraud, and auditing EU funds use are assigned to organisational units and institutions within the system of the indirect management of EU funds in the Republic of Serbia. One of the key weaknesses the PFMRP 2021–2025 seeks to rectify is the lack of technical administrative capacities in the organisational units and institutions pertaining to this system of the indirect management of EU funds.

Finally, under the PFMRP 2021–2025, the National Assembly will continue to develop its control function over public finances. Its Committee on Finance, State Budget, and Control of Public Spending is tasked with discussing State Audit Institution reports in the presence of representatives of the State Audit Institution and auditees, and, as and when required, representatives of other relevant central- and local-level bodies, organisations, and institutions. To strengthen the parliamentary oversight of public finances, the Committee will monitor the implementation of measures listed in the conclusion of the National Assembly on the occasion of the adoption of the State Audit Institution's Operating Report.³⁵ Further to the steps taken to enhance Parliament's oversight function with regard to the executive power performance, the Parliament Committee began organising public hearings for the presentation of the Draft Budget System Law and the Draft Act on Final Account of the Budget. The objective of these public hearings is to collect relevant information and expert opinions on the draft laws and clarify any of their proposed features. In accordance with the PFMRP 2021–2025, the first public hearing for the 2023 Draft Budget System Law and the Draft Act on 2021 Final Account of the Budget was held in December 2022.

6. Concluding remarks

The public finance system in the Republic of Serbia has undergone significant changes in recent years, aiming to achieve further alignment with EU rules. Although the Serbian system is not fully aligned with EU law, the reforms implemented thus far were estimated to be sufficient for the opening of EU-Serbia negotiation chapters pertaining to the area of public finance. Negotiations on Chapter 5 on public procurement were opened in December 2016; negotiations on Chapter 17, which is dedicated to economic and monetary policy, were opened in December 2018; negotiations on Chapter 29, which relates to the customs union, were opened in June 2017;

³⁵ Ibid., p. 87.

negotiations on Chapter 32 on financial control were opened in December 2015; and negotiations on Chapter 33, which covers financial and budgetary provisions, were opened in June 2018. Following the reform of the EU's enlargement methodology, the negotiations related to the public finance system are now part of Cluster 1, entitled 'Fundamentals'.

Under the general fiscal rules prescribed by the BSA, government sector debt, including the liabilities based on restitution, should not exceed 60% of GDP, and the target medium-term fiscal deficit should represent no more than 0.5% of GDP. According to the principles of responsible fiscal management, employee expenses in the government sector must be fixed at a sustainable level, with efforts made to keep the share of these expenses in the GDP at under 10%. Although the budgetary procedure is well designed, the 'regular' path for budget adoption was not always observed in the past, mainly due to economic perturbations caused by the COVID-19 pandemic. The two 2021 amending budgets were adopted via urgent procedures, whereas the 2022 budget was adopted in line with the normal legislative procedure, which included a series of parliamentary debates. The Fiscal Council was also consulted in the process. Moreover, budget transparency needs to be improved. No transparency roadmap, prebudget statement, or mid-year report has been produced or published. The Ministry of Finance does not publish the budget execution profile at the beginning of the year, which prevents any analysis of deviations from targets. Some additional policy and fiscal risk information could be included in the executive's budget proposal. The transparency of local budgets has been improved by the introduction of budget portals in 21 cities and municipalities in Serbia, which have enabled councillors in the local assemblies, as well as citizens, to monitor the preparation and spending of the budgets throughout the year and to actively participate in these processes. Finally, the link between the government programme and the sector strategies and operational plans of budget beneficiaries remains weak.

In Serbia's 2022 EU Progress Report, the European Commission insisted that Serbia should contain overall spending on wages as a percentage of GDP and take preparatory steps toward an appropriately designed public sector wage system reform.³⁶ The public wage increases exceeded nominal GDP growth in three consecutive years, leading to an increase in the wage bill from 9.0% of GDP in 2017 to 10.5% in 2020. The share decreased to 10.0% in 2021 owing to very high nominal GDP growth. The wage system reform has been postponed until 2025. The European Commission also emphasised that the annual ceiling for the overall general government fiscal deficit does not appear to be sufficiently transparent and operational. There are no adequate sanctions in the case of non-compliance, nor effective enforcement mechanisms.³⁷

³⁶ Commission Staff Working Document, Serbia 2022 Report, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, COM(2022) 528 final, p. 67.

³⁷ Ibid., pp. 70–71.

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