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**Working Paper**

## EU integration and the introduction of State aid control in Serbia: Institutional challenges and reform prospects

Discussion Paper, No. 1/16

**Provided in Cooperation with:**

Europa-Kolleg Hamburg - Institute for European Integration

*Suggested Citation:* Milenkovic, Marko (2016) : EU integration and the introduction of State aid control in Serbia: Institutional challenges and reform prospects, Discussion Paper, No. 1/16, Europa-Kolleg Hamburg, Institute for European Integration, Hamburg

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**Discussion Paper  
No 1/16**

**“EU integration and the introduction of State aid control in Serbia – institutional challenges and reform prospects”**

Marko Milenkovic

January, 2016

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Europa-Kolleg Hamburg, Institute for European Integration, Discussion Paper No 1/16,  
<http://www.europa-kolleg-hamburg.de>

**“EU integration and the introduction of State aid control in Serbia – institutional challenges and reform prospects”**

Marko Milenkovic\*

**Abstract**

Serbia’s EU integration has gained momentum after political change in 2000. From that point, numerous EU initiatives have been employed to facilitate the country’s legal, economic and political change in order to prepare it for (potential) EU membership. The cornerstone of the relations between the country and the EU is the Stabilisation and Association Agreement, which mandates the full alignment of state aid measures to EU standards.

Since 2006, subsequent governments have been working on aligning the substantive rules for the granting of state aid to the (ever-changing) EU framework, with a growing number of state aid measures and schemes being notified to and approved by the Commission for State Aid Control. However, this period was also characterised by a severe economic crisis that created the challenge for the Serbian government of aligning with the EU state aid regime, on the one hand, and facing pressure to save failing banks and companies, and prevent job losses, on the other.

By examining the institutional structure of the regime’s control body and the overall experiences of the first phase of the implementation of the Law on State aid, this paper draws conclusions on the major challenges and obstacles to introducing a new regulatory regime in the context of a deep economic crisis, ongoing enlargement fatigue and conflicting political legacies.

**Keywords**

Serbia, State aid, legislative transformation, institutional independence, integration challenges, conditionality, enlargement fatigue.

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## **1. Introduction: State aid control - a cornerstone of economic reform in a transitional economy?**

With a unique set of rules and developed practice of State aid scrutiny in the internal market, which is unparalleled globally, the EU has developed, over the past decades, a framework<sup>1</sup> that generally prevents governments from aiding individual companies, but also allows aid to companies in order to achieve multiple societal purposes. This unique kind of approach particularly was a novelty for transitional countries that were shifting from the old paradigms of planned economies in which state interference in the economy and aid to otherwise unsustainable undertakings was the norm.<sup>2</sup>

Serbia's EU integration has gained momentum following the political change in 2000. Since that point, numerous EU initiatives have been employed to facilitate the country's legal, economic and political change, and to prepare it for (potential) EU membership. The cornerstone of the relations between the country and the EU is the signing (in 2008) and entry into force (in 2013) of the Stabilisation and Association Agreement (SAA), which mandates the full alignment of State aid measures, within a four-year period, to EU standards. This was also envisaged by the Interim Trade Agreement (ITA) concluded at the same time as the SAA, which entered in force in January 2010, and thus, the deadline has effectively passed. The Law on State Aid was adopted in 2009 and was applicable as of January 2010. Since 2006, subsequent governments have been working on aligning the substantive rules for the granting of state aid to the (ever-changing) EU framework, with a growing number of State aid measures and schemes being notified and approved by the Commission for State Aid Control. However, this period was also characterised by a severe economic crisis that created the challenge for the Serbian government of aligning with the EU state aid regime, on the one hand, and pressure to save failing banks and companies, and prevent job losses, on the other.

Although the observed period (the first five years of the Law's implementation - 2009-2014) points to a shift in the State aid paradigms within the EU itself, the paper examines the hypothesis that, over a given period, the measures adopted in Serbia in the field of State aid

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<sup>1</sup> State aid granted by individual member states was, from the onset, in the focus of European Union competition policy, together with other obstacles preventing free market competition. For an overview of EU State aid law and policy, see: Heidenhaim (2010), Jones and Sufrin (2013), Jovanovic (2013).

<sup>2</sup> For an analysis of the transition from a planned to a market economy, see *inter alia*: Gros, Steinherr (2004).

demonstrate, to certain degree, a willingness to approximate the rules and implement the *acquis*, but also that successive governments have struggled to change their economic policies in the context of the crisis and to dismantle, both politically and legally, state interference in the market. It will further explore the hypothesis that the Serbian State aid control system has an inherent weakness in its institutional structure. Namely, the Commission for State Aid Control – which is supposed to be an independent control body – is made, to a great extent, dependent on the Ministry of Finance in preparing decisions and monitoring State aid grantors. The paper will explore how this institutional arrangement, coupled with the limited administrative capacities that are available, has prevented the Commission from achieving more in terms of the scrutiny of State aid in Serbia. Although comparative examples in transitional countries point to various models of State aid control bodies, some of which are very similar to that in Serbia, in this paper, we argue that it is necessary to have a fully independent and operational body in a given societal context in order to drive the reforms and align the legislation with the State aid framework in the absence of the European Commission acting as a watchdog.<sup>3</sup> The paper also analyses whether the existing Commission for Protection of Competition would be a suitable body to be granted new tasks in controlling State aid, as has been the case in some other Central and Eastern European countries.

Scholarship on State aid in Serbia is still relatively limited. This paper aims to fill this gap and to enable competition scholars and practitioners to address the reform process that has been taking place in Serbia (and the region). By employing the analytical concepts of governance by conditionality (and external governance), we examine the factors influencing the legal change in this particular context. This analysis is based on: a) a review of comparatively and contextually relevant literature, b) a review of the Serbian legislative framework, and c) interviews to collect relevant data. The set of interviews was conducted with experts involved with the regime in Serbia so as to gain qualitative data and insight into the most pressing problems in the process of the introduction of State aid control and the current challenges in the context of economic hardship and slow recovery.

In the first part of the paper, we analyse the conditionality approach in the European integration process. By providing an overview of the main theoretical dilemmas on conditionality and its usage in the process of the integration of transitional countries, we are looking into the

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<sup>3</sup> In Serbia, as in other transitional countries, the association agreement envisages the establishment of an independent national monitoring and control body *prior* to joining the EU.

significance of this approach in changing economic governance.<sup>4</sup> In the second part, we provide an overview of the introduction of State aid in Serbia, giving a brief account of the relevant legislation, but also describing and analysing the main impediments in the process. In the third part, our attention is directed towards an analysis of the institutional setting for the control of State aid measures in Serbia. Finally, drawing on the analysis in the previous parts, we offer conclusions and policy recommendations for decision makers which we believe might be of use in the future approximation of the State aid regime.

## **2. The Europeanisation of the Western Balkan countries and governance by conditionality**

The political, legal and economic transformation of the Western Balkans over the past two decades was mostly EU driven. No other region has been subjected to such a numerous and challenging conditionality prior to joining. The reason for this is twofold. On the one hand, there is a legacy of ethnic conflicts and civil wars in the region that make the post-war reconstruction and reconciliation far more complicated and especially sensitive in comparison to the usual hardships associated with the economic transition and transformation towards a market economy which have been typical of Eastern and Southeastern European countries. The other reason is the fact that the Western Balkan countries, as the last to join the European Union, must undergo a profound check test and must fulfil a much larger set of requirements to join, compared to previous entrants to the EU. This includes the building up of conditionality requirements based on the experiences of the previous grand enlargement of 10 new member states in 2004, and especially, the entry into the EU of Bulgaria and Romania in 2007.<sup>5</sup> These enlargements have shed light on all of the risks of the “unpreparedness” of individual countries to “join the club”, and thus, Western Balkan (WB) societies are being required to undertake “by the book” transformative processes in order to fulfil the requirements. This is especially the case for State aid control.<sup>6</sup>

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<sup>4</sup> State aid was first contextualised as an accession criterion more than 10 years ago by Schutterle: (Schutterle 2002 a,b)

<sup>5</sup> For some accounts of unpreparedness for the membership, see: Kochenov (2014), Jovanovic (2013).

<sup>6</sup> As was pointed out by a State aid advisor to Romanian authorities just before the accession: The “European Commission has, in its Reports on Romania's progress towards accession, regularly identified State aid control as one of the 'problem areas' which could possibly give rise to a delay in the closure of the accession negotiations and - once they have been duly closed - even on the date of accession.” (von



## 2.1. Defining conditions and the conditionality approach

The Europeanisation literature has widely analysed the approach of governance by conditionality which was implemented with respect to the Central and Eastern Europe (CEE) entrants into the EU and which has reached an unprecedented level in the case of the Western Balkan countries. Presenting the results of a collaborative research study undertaken on EU rule transfer, Schimmelfennig and Sedelmeier argue that “rule transfer is best explained by an external incentives model of governance; its effectiveness varies with the credibility of EU conditionality and the domestic costs of rule adoption.” As they put it: “The desire of most CEECs to join the EU, combined with the high volume and intrusiveness of the rules attached to its membership, have allowed the EU an unprecedented influence on the restructuring of domestic institutions and the entire range of public policies in these countries. A key difference between the internal and the external dimension of governance is that, while the former primarily concerns the *creation* of rules, as well as their implementation in national political systems, the external dimension is exclusively about the *transfer* of given EU rules and their adoption by non-member states.” (Schimmelfennig and Sedelmeier 2004, 661) “The very nature of the accession negotiations (structured around the need for full compliance with the EU’s *acquis communautaire*) coupled with their extremely tight timeframe and profound power asymmetries between the negotiating parties have unleashed a massive pressure for domestic adaptation across Central and Eastern Europe. This process has often been referred to as ‘Europeanisation’.” (Papadimitriou and Gateva 2009, 4) The principle of conditionality - one of the key components of the EU’s strategy in post-communist Central and Eastern Europe - is widely acknowledged to be the driving force behind the process of enlargement-led Europeanisation. (Papadimitriou and Gateva 2009, 5)

Up until the beginning of the 1990s, previous rounds of EU enlargements were carried out *ad hoc* and not with a set group of criteria to be fulfilled by the aspiring applicants. The procedure was legally based on the treaty provisions in a process which was mostly member-state driven. (Hillion 2011) The rules for conducting accession have remained limited to date, as there is no specific secondary legislation, but rules and procedures have been developed by the practice of the institutions, with growing pre-entry conditions. The conditions were broadly formulated only when the enlargement to the Eastern countries commenced in 1993, and the conditionality itself has been gradually built up. (Anastasakis and Bechev 2003, 5) The Copenhagen criteria were

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Borriers 2006, 509) This did not take place in the Romanian case, as further assessments were better, but it provides a picture of the magnitude of the challenge it may pose in the WB countries’ integration.

formulated in 1993 as follows: 1) Stable, democratic institutions, the rule of law, respect for human and minority rights (political criteria); 2) A functioning market economy and the ability to withstand competition from EU companies (economic criteria); and 3) The ability to assume the responsibilities of membership (legal harmonisation).<sup>7</sup> As it became apparent that the fulfilment of those three criteria would be conditional on having a proper civil servant corps that is able to transpose the new rules in the accession countries, the institutional capacity criterion was added by the Madrid Council in 1995. (European Council 1995) These criteria were then further elaborated by the European Council in subsequent years.<sup>8</sup>

## 2.2. Stabilisation and Association Process (SAP)

The Stabilisation and Association Process (SAP) was introduced as a regional approach for the Western Balkans in 1999, right after the conflict between the Federal Republic of Yugoslavia and NATO had ended, in order to facilitate the integration of the WB region and to serve other EU policy goals beyond reconciliation in the region. As the former Federal Republic of Yugoslavia was under the regime of Slobodan Milošević and subject to sanctions by the international community, it was not initially included in the SAP, but joined it immediately after the political change in 2000. The process is comprised of four components: 1) political dialogue; 2) pre-accession aid; 3) autonomous trade measures; and 4) Stabilisation and Association agreements (SSA). In our previous work, we pointed out two types of conditionality used to further progress in European integration—one that arose on a contractual basis (and stemming from the SSAs and the adoption in full of the *acquis*) and another that appeared as a consequence of *ad hoc* political conditioning at a particular moment of integration. (Milenkovic and Milenkovic 2013a)

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<sup>7</sup> (European Council 1993) Anastasakis and Bechev point to four different types of conditionality for the WBs in addition to Copenhagen criteria,—regional; country-specific conditions related to individual projects; grants or loans; and those arising from peace agreements and political deals (for example, Resolution 1244 of the UN Security Council) (Anastasakis and Bechev 2003, 7–8). They also refer to conditionality as: The “EU’s most powerful instrument for dealing with the candidate and potential-candidates countries in post-communist Europe” (Anastasakis and Bechev 2003, 3). Balazs distinguishes between written conditions, unwritten conditions and “additional preconditions”. (Balazs 2014)

<sup>8</sup> For a detailed overview of the development of the enlargement *acquis*, see: Handbook on Enlargement (2002), Tatham (2009), Hillion (2011).

Stabilisation and Association agreements are international agreements between the EU, its member states and potential candidates, which primarily focus on trade liberalisation and the gradual creation of a free trade area. Up until entry into force of the accession agreements, they remain the main contractual basis for relations between the Union and the countries concerned. In addition to trade provisions providing the widest and most privileged access to the EU market for goods from the countries, it also provides a set of other legal and political reforms with precisely set time limits for the implementation of legislative transformation. This enables the EU Commission to further monitor the progress of reforms in the country during the integration period. Among the provisions included in these agreements are obligations to perform reforms in the sphere of competition policy and State aid control. As we will demonstrate in the forthcoming pages, this has proven to be more than challenging in a number of new member states, given the legacy of their pasts and tradition of planned economy.

As a part of the process, and as the political decision was made to enable enlargement to the Western Balkan countries in 2003, potential candidates can apply for EU membership and can be approved as a candidate country by the European Council. (European Council conclusion Thessaloniki 2003) This happened only a year before the big enlargement of 2004 and three years before the entrance of Romania and Bulgaria – two countries that were lagging behind in reforms. In their study of the integration of Romania and Bulgaria, as two Balkan countries, Papadimitriou and Gateva discussed how the EU sought to influence domestic reform in the two countries through a mixture of threats and rewards. It is not difficult to claim that the example of Romania and Bulgaria should be watched and compared when discussing the integration of the Western Balkans, at least in terms of their economic reforms and their fight against corruption. As Papadimitriou and Gateva claim, “the case of the 2007 entrants offers three theoretically-informed insights into the process of EU enlargement: *firstly*, it highlights the evolutionary nature of enlargement conditionality and presents evidence of policy learning across different waves of EU enlargement; *secondly*, it demonstrates the difficulties surrounding the consistent application of conditionality towards ‘exceptional’ candidate countries (whether defined in cultural, historical or security terms); and, *thirdly*, it problematises the causalities between conditionality and domestic reform.” (Papadimitriou and Gateva 2009, 7)

However, upon the enlargements of 2004 and 2007, and the negative experiences of those accessions, enlargement fatigue is more than present in the approach of the institutions and the individual member states. It is further perpetuated by an increasing and changing

conditionality,<sup>9</sup> and it also raises doubts about whether the approach has reached its limits with unpredictable membership prospects. As was argued by Hillion: “The EU and its Member States thus used the membership promise as a bargaining chip to influence, if not steer, the structural reforms with a view to ensuring that the newcomers would be as amenable to membership as possible. In becoming itself a key actor of the transformation process, the EU entered uncharted territories of liberal democratic and market economy state-building....The inflated and evolving normative basis for enlargement has raised issues of double standards that have consequently undermined the credibility of the Union’s commitments to the norms and values it has advocated vis-à-vis the applicants, questioned the legitimacy of its conditionality, and ultimately the effectiveness of the transformation agenda”. (Hillion 2011, 195-196) As argued by Haughton: “Conditions can be set in different periods of integration, but they are most successful in moments when there is a need to make decisions within the integration process; for example, whether or not to open accession negotiations” (Haughton 2007). However, as Kochenov argues regarding conditionality: “[O]ne should be very careful in judging the effectiveness of the principle, particularly so, in the context of the self-congratulatory rhetoric of the EU institutions, which is often unfounded”. (Kochenov 2014, 542) Indeed, the Commission is ready to praise the conditionality approach as strict but fair; but there is a mixed review in the literature in regard to its effectiveness.<sup>10</sup>

Although Croatia was the first of the Western Balkan countries to join in the midst of economic recovery and fatigue, it has been clearly outlined by the head of the EU Commission that no further enlargement is foreseen for the mandate of the current Commission, which ends in 2020.<sup>11</sup> As we have already put forward elsewhere<sup>12</sup>, the lack of EU prospects will only create more difficulties in the Serbian case, as the elites will not be fully motivated to undertake reforms, and therefore, conditionality, especially in difficult and challenging fields such as State aid, may well fail to bring results. As accession perspectives and the context of the integration have changed dramatically for governments struggling to deal with the consequences of the economic

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<sup>9</sup> For an analysis of the flaws of conditionality, notably in the enlargement context: Kochenov (2009).

<sup>10</sup> See further: Kochenov (2014)

<sup>11</sup> Eubusiness, “Juncker to halt enlargement as EU Commission head”, 15 July 2014, <http://www.eubusiness.com/news-eu/politics-juncker.x29>

<sup>12</sup> Milenkovic Milos, Milenkovic Marko (2013 a,b)

crisis, which are strongly felt in the region, the EU's pressure power has been lost to a great extent.

Finally, the EU is facing another problem with the conditionality approach which is vested in the very nature of the "reward" that may be offered to potential candidates (as it has been referred to by many of the actors involved in the process). In addition to the visa-free regime, pre-accession aid (limited in amount and effect) and trade liberalisation, there is little else that the EU may offer except full membership. Countries in the region have already received all of these rewards and have free trade regimes guaranteed by international agreements with the EU and the member states. There are, of course, some smaller rewards that might be interesting to a limited number of citizens in the applicant countries, such as cultural and scientific programmes, but they are limited in both their scope and incentive effect, as they are not attractive to the majority of the electorate and the politicians.

Having this troublesome policy dilemma/limit of conditionality, we will proceed to an overview of the transformation of the competition and State aid regimes in the context of EU enlargement in general.

### **2.3. Transformation of competition and State aid regimes in the context of EU integration – conditionality put to the test**

The integration of the countries of the former communist bloc, which were dominated by planned economies, has posed a political challenge for the EU integration process since the late 1980s, when it was clear that political change was about to happen which would have far-reaching consequences for the EU and its member states.<sup>13</sup> The introduction of the competition and State aid regimes proved to be particularly challenging in the transition process, as the countries of Eastern and Central Europe had to leave behind their legacy of planned economies and state (over)interference in market relations.<sup>14</sup> Therefore, the approximation of laws in this area has been particularly challenging, given the fact that the countries of Eastern Europe had not participated

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<sup>13</sup> For an overview of the relations of the EU with the CEE countries, see *inter alia*: Sedelmemeier and Wallace (2000)

<sup>14</sup> For some accounts of the transformation of competition regimes in the region, see *inter alia*: Emmert (2003).

in the trend toward trade and economic liberalisation after the Second World War.<sup>15</sup> All of the countries acceding to the European Union today have an obligation to introduce State aid control regimes. This obligation had already been foreseen for the countries which acceded in 2004 and was stipulated in their respective European Agreements.<sup>16</sup> A similar obligation is foreseen for the Western Balkan countries through the far-reaching Stabilisation and Association agreements mentioned above.

This transition was lengthy for the countries of Central and Eastern Europe, and it included changes in their competition and State aid regimes. In 2001, in Laeken, the European Council concluded that all of the candidate countries had completed the transition from centrally planned economies to market economies and had fulfilled the criteria (except Bulgaria and Romania). (Schutterle 2002, 585) It has been argued that “[t]he sophisticated set of the EU *acquis* is the fruit of West[ern] European legal and institutional development of well established market economies and parliamentary democracies”. (Balazs 2014, 526) Therefore, this approximation required not only economic, but also great political and cultural change. (Milenkovic 2010)

Having lost the pace of integration and lagging behind the other transitional countries, the Western Balkan societies are now facing the task of aligning their regimes with EU norms.<sup>17</sup> In his analysis of State aid enforcement in the Western Balkan region, Botta has also come to the conclusion that the lack of clear timing for EU accession has hampered the degree to which State aid rules have been enforced; in addition, his analysis of the enforcement records indicates that State aid control should be exclusively carried out at the supranational level prior to accession. (Botta 2013, 83)<sup>18</sup> Conditionality is mostly examined in the context of political reforms and the associated pressures on aspiring candidates that stem from the existing member states or the Union as a whole. However, in light of enlargement fatigue, combined with the economic crisis, it is our presumption that economic conditionality will play a much more prominent role in the WB enlargement. It was already present in the clauses which the new members were required to

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<sup>15</sup> However, the former Yugoslavia was a notable exception, with its specific socialist self-governance system, which was much more open to foreign trade than the countries of the communist bloc.

<sup>16</sup> For State aid provisions in the European agreements and SAAs, see: Cremona (2003). The first reference to State aid *acquis* was in the case of Poland and was made as early as 1991 in the European Agreement. (Paczkowska-Tomaszewska, Jaros, Winiarski 2006, 669).

<sup>17</sup> For an overview of the early development of State aid regimes in the region, see: Schutterle (2005); Evans (2004).

<sup>18</sup> In our opinion, this finding needs further consideration and will be addressed through a follow-up qualitative study.

adopt, giving their consent for their citizens not to be allowed into the labour markets of all the old member states from the date of accession. So, having these processes in place, it is expected that more conditionality will come, not only as a consequence of identity issues and past conflicts (with which the WB abounds), but also in a range of economic fields reflecting the particular interests of the member states. Some of these conditionalities might even be “hidden cultural conditionalities” (Milenkovic Milos, Milenkovic Marko 2013a) that are not put forward formally, but are conceived under the formal requirements, for example, to dismantle a State aid scheme covering a competitor of an important undertaking for a member state. As was already noted, there are around 1980 obstacles on the road to membership (Jovanovic 2013), with every member state (MS) giving consent, and possibly, blocking every single step in the integration process. With the ongoing crisis, which has left a strong mark on the economies of Europe, we can only presume the role that State aid conditionality might actually have in the years to come.

### **3. Introduction of the State aid control regime in Serbia**

The National Reports on State aid which Serbia has comprised since 2004 point to a relatively high level of State aid compared to GDP.<sup>19</sup> The process of the drafting and adoption of the Law on State Aid took several years. First, it was led by the Treasury department of the Ministry of Finance. A group of three civil servants was first tasked with composing reports on the State aid granted in Serbia in 2004, using a methodology provided by the European Commission. As pointed out by the informants, this was pioneering work, as only a handful of civil servants were aware of the magnitude of the reforms to be undertaken in this field, and there were very few experts in the country who were familiar with the specificities of the EU regime. Several international consultants and experts were deployed in the process of drafting of the law, and consultations were made on the appropriate choice of an institutional framework for the implementation of the Law.<sup>20</sup>

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<sup>19</sup> For years, it has amounted to more than 2% of GDP as compared to the 0.5% usually granted through subsidies in EU member states. Reports are available in English at: <http://www.mfin.gov.rs/pages/issue.php?id=9850>

<sup>20</sup> It is possible to observe a clear influence of the Slovenian model on the Serbian institutional setting, as the Slovenian’s State aid chief at the time was consulting with Serbian authorities. It was also stressed by one of the informants that consultants from the region had the largest impact on the reforms. This is quite expected, as the use of models and advice from colleagues coming from the same administrative background and who speak the language is always beneficial for recipients of technical aid.

After several years of preparation, with the enactment of the Law, the basic substantial, procedural and institutional rules were put into place. It envisaged that the Government would form a State Aid Control Commission entrusted with controlling all individual State aid measures and schemes. By virtue of the law, no aid may be granted without a prior decision by the Commission. The Law was adopted in July 2009 and prescribed its entry into force on 1 January 2010. The Law was adopted as a part of a reform package, together with the new Law on Competition. Given this simultaneous adoption, it did not receive a great deal of public attention, as all eyes were focused on the new composition of the Commission for Protection of Competition and the changes that enabled the Commission to directly sanction breaches of the competition rules. The members of the Commission for State aid control were appointed in December 2009 according to the law by a Decision of the Government, just days before the envisaged beginning of the implementation of the new regime in the country, leaving very little room for preparations to be made for the commencement of the implementation of the control mechanisms.

The five-year period (2009-2014) provides room for a first analysis of the achievements of the national State aid control system, the functioning of the institutions and the overall level of the approximation of the national rules and practice to EU law. Some analysis has already been provided by the civil sector; it is mainly critical, pointing to observed weaknesses in terms of both the legislative framework and the institutional design and independence.<sup>21</sup> However, we observe that the starting point of the analysis needs to be the regulatory intentions of the decision makers while they are establishing the system. They are, without doubt, that the system is introduced to: 1) fulfil the obligations arising from the international agreement (SAA); 2) prevent the distortion of competition regarding trade among the EU member states (MS) and Serbia; 3) prepare the candidate country's administration to be able to implement the EU regime once the country becomes a part of the internal market, and last but not least; 4) prevent distortions in the competition among the undertakings in the Serbian market. This last objective, which might be recognised in the Law on State Aid, is of utmost importance in the national context, but it is not a priority in terms of European integration, as EU law in this area is aimed at preventing the distortion of competition among the member states. As the economic output of Serbia and the GDP of Serbia are small compared to developed European economies, the effects of the distortions caused by most State aid measures in Serbia are very local in their effects.

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<sup>21</sup> Transparency Serbia (2015).



### 3.1. Stabilisation and Association Agreement obligations to harmonise State aid rules and the first implementation obstacles

The Serbian Stabilisation and Association Agreement contains provisions on the approximation of laws, law enforcement and competition rules following the structure of the Treaty on the Functioning of the European Union.<sup>22</sup> Article 73 provides that the following are incompatible with the proper functioning of this Agreement, in so far as they may affect trade between the Community and Serbia: (i) all Agreements between undertakings, decisions by associations of undertakings and concerted practices between undertakings which have as their object or effect the prevention, restriction or distortion of competition; (ii) abuse by one or more undertakings of a dominant position in the territories of the Community or Serbia as a whole or in a substantial part thereof; (iii) any State aid which distorts or threatens to distort competition by favouring certain undertakings or certain products. It further prescribes that any practices contrary to this Article shall be assessed on the basis of *criteria arising from the application of the competition rules* applicable in the Community, in particular, from Articles 81, 82, 86 and 87 of the EC Treaty<sup>23</sup> and the interpretative instruments adopted by the Community institutions.<sup>24</sup> This adherence to the omnipresent interpretative instruments adopted by the EU institutions includes those not in force at the time of the signing of the SAA, without any possibility for the association country to influence its content.<sup>25</sup>

According to the SAA, the parties shall ensure that an operationally independent authority is entrusted with the powers necessary for the full application of paragraph 1(i) and (ii) of this Article, regarding private and public undertakings and undertakings to which special rights have been granted. In Serbia, this is done by the Commission for Protection of Competition. It is also

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<sup>22</sup> Available at: <http://www.seio.gov.rs/documents/agreements-with-eu.216.html>

<sup>23</sup> As the SAA was negotiated and signed prior the entry into force of the Lisbon Treaty, it contains the old numeration and refers to the EC Treaty.

<sup>24</sup> As observed by Cremona, it was a very specific condition built into SAA treaties requiring the parties (candidates for membership) to observe and implement all of the soft law provisions in which this area of the EU abounds. (Cremona 2003)

<sup>25</sup> Assessing this kind of provision back in 1998, the Constitutional Court of Hungary reasoned that “the Republic of Hungary is an independent democratic state governed by the rule of law”, and as such, its authorities cannot be bound – without violating its sovereignty – by [the] norms and practice of another public order, namely the European Union.” (Knapp 2014, 228) This kind of challenge has still not been brought to the Serbian Constitutional Court, but given the fact of the growing enlargement fatigue and the unlikelihood of Serbian accession, it is plausible to expect it.

envisaged for Serbia to establish an operationally independent authority which is entrusted with the powers necessary for the full application of paragraph 1(iii) within one year from the date of entry into force of this Agreement. This authority shall have, *inter alia*, the powers to authorise State aid schemes and individual aid grants in conformity with paragraph 2, as well as the powers to order the recovery of State aid that has been unlawfully granted.

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

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

For the purposes of applying the provisions of paragraph 1(iii), the parties recognise that during the first five years after the entry into force of this Agreement, any public aid granted by Serbia shall be assessed taking into account the fact that Serbia shall be regarded as an area identical to those areas of the Community described in Article 87(3)(a) of the EC Treaty, which is a standard for all of the countries in the region.<sup>26</sup>

Within four years from the entry into force of this Agreement, Serbia is bound to submit to the European Commission its GDP per capita figures, harmonised at the NUTS II level.<sup>27</sup> The authority referred to in paragraph 4 of Article 73 (now the State Aid Commission) and the European Commission shall then jointly evaluate the eligibility of the regions of Serbia, as well as the maximum aid intensities in relation thereto in order to draw up a regional aid map on the basis of the relevant Community guidelines. This still remains to be done.

It is further envisaged for State aid provisions not to be applicable to agricultural products. The separate Protocol 5 to the SAA establishes the rules on State aid in the steel industry. This

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<sup>26</sup> See further: Botta (2013).

<sup>27</sup> For details regarding the Nomenclature of territorial units for statistics (NUTS), see further: <http://ec.europa.eu/eurostat/web/nuts/overview>

Protocol establishes the rules applicable in the event that the restructuring of aid is granted to the steel industry.<sup>28</sup>

By the virtue of Protocol 5 on State Aid to the Steel Industry, the parties “recognise the need that Serbia addresses promptly any structural weaknesses of its steel sector to ensure the global competitiveness of its industry”. It was also prescribed that the Community recognises that, for five years after the entry into force of this Agreement, Serbia may exceptionally grant State aid for restructuring purposes to steel producing firms in difficulty, provided that: (a) it leads to the long-term viability of the benefiting firms under normal market conditions at the end of the restructuring period; (b) the amount and intensity of such aid are strictly limited to what is absolutely necessary in order to restore such viability, and aid is, where appropriate, progressively reduced; and (c) Serbia presents restructuring programmes that are linked to a global rationalisation which includes the closing of inefficient capacity. Every steel producing firm benefiting from restructuring aid shall, as far as possible, provide for compensatory measures balancing the distortion of competition caused by the aid. Serbia has also agreed to submit a National Restructuring Programme and individual business plans for each of the companies benefiting from restructuring aid which demonstrates that the above conditions are fulfilled to the European Commission for assessment.<sup>29</sup> The five-year period passed at the beginning of 2015, bringing a completely different realm to Serbia’s traditionally state-subsidised steel industry.

Finally, it was envisaged that nothing in Article 73 shall prejudice or affect in any way the taking, by the Community or Serbia, of countervailing measures in accordance with the GATT 1994, the WTO Agreement on Subsidies and Countervailing Measures and the respective related internal legislation.

The SAA also contains provisions on public undertakings in Article 74 and stipulates that, by the end of the third year following the entry into force of this Agreement, Serbia shall apply the principles set out in the EC Treaty to public undertakings and undertakings to which special and exclusive rights have been granted, with *particular reference to Article 86*. Special rights of public undertakings during the transitional period shall not include the possibility of imposing quantitative restrictions or measures having an equivalent effect on imports from the Community into Serbia. The EU *acquis* in this area includes provisions on the transparency of financial transactions

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<sup>28</sup> It is further envisaged that such aid would have an exceptional character, would be limited in time and would be linked to capacity reductions within the framework of the feasibility programmes.

<sup>29</sup> For the full text of the Protocol, see: Serbia Stabilisation and Association Agreement (2008).

between member states and public undertakings<sup>30</sup> which are enacted by the Commission on the basis of the powers provided by Article 106 TFEU (formerly Article 86 TEC). Serbia is legally bound to implement the standards put forward in this legal act, which presents major cultural and economic changes in the context of the tradition of nontransparent relations between the government and public undertakings,<sup>31</sup> and will, according to the informants, continue to be a challenge in the implementation of the regime.

One of the main questions put forward to the informants during the qualitative research was whether competition and State aid experts in Serbia (mostly academics during that time) were consulted when the deadlines, for example, for composing inventories, were negotiated. To the best of their knowledge, there were very few consultations, and furthermore, very little room for a Serbian delegation to negotiate different timeframes and deadlines for certain obligations other than those put forward by the European Commission. This especially refers to the deadlines in Protocol V concerning steel products. As one of the informants claimed, “we were very much presented with the model agreements prepared for all the countries in the region”, and therefore, there was no room to negotiate.

One of the biggest challenges for the Government has been to produce a detailed inventory of all State aid schemes existing in the country. This obligation was not fulfilled in the previous period and is expected to remain one of the main conditions in this field until finalised. Although Serbia has a substantial amount of time prior to accession (if it ever occurs), it is still necessary as a part of SAA. Member states that joined the EU in 2004 had a relatively short period to implement State aid regimes, and therefore, their inventories of existing aid were submitted to the Commission, but in some cases, were not approved even after the accession to the EU.<sup>32</sup> It remains to be determined what will be considered to be existing aid in the context of the negotiations in this case (of Serbia).

The implementation of ITA began in January 2010, leaving little room for the Commission and the Ministry of Finance department to prepare for the process. In addition to this time-constraining initial period, it is of crucial importance to view the analysis from the perspective of

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<sup>30</sup> Commission Directive 2006/111/EC of 16 November 2006 on the transparency of financial relations between Member States and public undertakings, as well as on financial transparency within certain undertakings. (OJ 17.11.2006, L 318, p 17).

<sup>31</sup> For more on the implementation of the transparency directive in the context of state aid, see: Heidenhaim (2010, 447-458).

<sup>32</sup> See further: Jagodic, Lekocevic, Pelka, Vosu (2004).

the negative economic trends in the region of the Western Balkans, and Serbia in particular, since the beginning of the economic crisis in 2008.<sup>33</sup>

### 3.2. The law on State aid control and the transposition of the EU regime

The Law itself basically transposes Treaty provisions and defines State aid according to the established approach of the Commission and the Court of Justice. The Law<sup>34</sup> regulates “the general terms and procedure for the state aid control with a view to ensure protection of free competition on the market, through implementation of the principles of the market economy and encouraging the economic development, transparency in the state aid granting, as well as fulfilling undertaken obligations related to international agreements that contain provisions on state aid”. Agricultural and fisheries products are excluded from the scope of the Law<sup>35</sup>. (Article 1) From the formulation in the first article of the Law, it is apparent that the intentions of the Law are twofold - both to protect free competition in the market and to fulfil international obligations (arising from the SSA, and in the future, EU and WTO law, once Serbia joins those organisations). The Law defines *State aid* as “any actual or potential public expenditure or realised decrease in public revenue which confers to [the] state aid beneficiary a more favorable market position in respect to the competitors and as a result causes or threatens to cause distortion of the market competition”.<sup>36</sup> As was already outlined, the Law transposes treaty provisions on categories of aid that are or may be allowed. It also contains a definition of “unallowed state aid”: “Regardless of the form in which it was granted, any state aid that distorts or threatens to distort market competition, other than different rule has not been laid down by this Law, or is contrary to internationally ratified treaties, shall be deemed unallowed”. (Article 3)<sup>37</sup>.

The Law does not contain detailed substantive norms on the types of aid that may be compatible/allowed. These are laid down in detail in the Regulation on the rules for the granting

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<sup>33</sup> Even before this crisis, the region was lagging far behind the European Union it wishes to join. For an overview of the economic development and hardship, see, *inter alia*: Jovanovic (2013).

<sup>34</sup> All of the formulations used in the paper are from the official translation of the law in English provided by the Ministry of Finance on the official web page: <http://www.mfin.gov.rs/pages/article.php?id=9641>

<sup>35</sup> However, since 2012, the Commission (and the Ministry) have started including data on agricultural subsidies and other aid measures in this field in the annual State aid reports.

<sup>36</sup> Article 2 of the Law (meaning of terms).

<sup>37</sup> N.B. Inaccuracy in translation into English, it should read “unless different rule has been set by this Law”

of State aid. As explained by the informants, the intention was to keep the law relatively “short and simple” and to allow for the substantive provisions to be changed more frequently in order to adhere and transform in accordance with regulatory changes in the European Union. The flexible way to do this, without going into the lengthy procedure of law amendments, was to allow the government to adopt bylaws setting the details of the substantive rules. Indeed, this approach has resulted in the Law remaining unchanged since its adoption in 2009, although the relevant bylaws have undergone multiple amendments, which have taken place once or twice a year since then.<sup>38</sup> The Law contains a number of provisions on the position and competences of the Commission which are described in detail in the next part, as well as detailed procedural rules.

It is prescribed that a State aid grantor shall be under an obligation to, before granting the State aid, notify the Commission of the State aid. (Article 11) The proposer of the regulation constituting the grounds for the granting of State aid shall, before forwarding it for adoption, notify the Commission of the draft and/or the proposal of such regulation. It has been underlined by the informants that, in a number of cases, legislative acts were adopted prior to the Commission being notified. This does not, however, imply that the aid envisaged would not have qualified as “allowed” or that an actual discharge of public funds for the incompatible measures has taken place. In the event of any changes to the notified State aid after the notification, the State aid grantor and/or the proposer of the regulation shall notify the Commission of such changes. The State aid grantor or proposer of the regulation is also entitled to withdraw the notification, in the capacity of a State aid applicant, before the Commission makes its decision. The State aid applicant is responsible for the truthfulness and correctness or accuracy of the information, in the sense of a complete State aid notification. (Article 11)

The Law envisages both *ex ante* and *ex post* control. The Commission commences the *ex ante* control upon receipt of a complete State aid notification. If the Commission finds that the notification does not “concern state aid”<sup>39</sup>, it shall adopt a decision where this is stated and shall inform the submitting party accordingly. If it finds that the notification “does concern the state aid”, the Commission shall decide whether the notified State aid is allowed within a period that cannot be longer than 60 days as of the date of receipt of the complete notification. If the applicant does not provide or refuses to provide the Commission with all of the requested information which

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<sup>38</sup> This has allowed for the introduction of rules on services of general economic interest and the changing of *de minimis* rules, so as to reflect legislative changes in the EU.

<sup>39</sup> N.B., Inaccuracy in translation into English, it should read - constitutes.

constitutes a complete State aid notification in the sense of this Law, the Commission shall adopt a decision *denying the State aid notification as incomplete*<sup>40</sup> and send it to the applicant. If upon receiving the complete notification, the Commission shall determine that the notified State aid is not contrary to the provisions of this Law, it shall adopt a decision which deems the State aid as allowed and send it to the applicant. If upon receiving the complete notification, the Commission shall determine that the notified State aid is fully or partially contrary to the provisions of this Law, it shall adopt a conclusion according to which the applicant is *assigned a deadline for correcting non-compliance*, with proposed measures for achieving compliance. If the applicant fails to act on the Commission's proposal, the Commission shall adopt a decision deeming the notified State aid as unallowed and send it to the applicant. This solution provides proof that the intention of the law is not to reject notifications, but rather to aid and correct the applicants' intentions. This adds to the hybrid nature of the Commission's role and position between independent watchdog and government body entrusted with certain administrative tasks, which will be analysed in a separate chapter. (Article 13)

Prior to the granting of State aid, the State aid grantor shall be required to send a copy of the Commission's decision that is relevant to the particular State aid beneficiary, or to inform the beneficiary of the manner and place where information can be received as to the content of such decision. (Article 14) This is important for beneficiaries in terms of legal certainty, but it still remains uncertain as to what extent the beneficiary is acting *mala fides* if it does not require such a decision before receiving State aid, and to what extent it could sue the grantor if ordered to return the aid received. As there have been no cases in which aid has been requested to be returned to date, how the beneficiaries would invoke this provision before the courts remains speculative.

The Law prescribes the standstill clause and prescribes that, until the adoption of the Commission's decision, namely, until the conclusion of the ex ante control, notified State aid cannot be granted. In the implementation of the Law, it has been especially problematic to prevent the grantors from actually discharging funds before the State aid measure/scheme has been approved by the Commission. In the first years of the implementation, that might have been attributed to grantors not being familiar with the particularities of the new regime and their obligations, but the continuation of such a practice after five years raises serious doubts regarding

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<sup>40</sup> Official translation.

the respect for the rule of law in the country. It will therefore present a challenge for the Government to put a stop to such a practice and to propose adequate accountability mechanisms to reverse this trend.<sup>41</sup>

The Law also provides for *ex post* control, which should, in general, be an exception rather than a rule. “The Commission shall conduct *ex post* control based on its own information or based on the information obtained from whatsoever source that suggests that it concerns the state aid that has been granted and/or is in use or has been used contrary to the provisions of this Law. Within further procedure of *ex post* control, the Commission shall order the state aid grantor to submit additional information and fix the deadline for submittal of such information.” The Commission shall conduct *ex post* control and take the decision based on the additional information, namely based on the available information, if the state aid grantor fails to act pursuant to the Commission’s order.<sup>42</sup> The Commission may order the State aid grantor to suspend the further granting of State aid if it finds that it would cause a more serious distortion to competition. (Article 16)

The Law also provides for the protection of the rights of the interested parties, namely, the competitors of the undertaking receiving the aid. Any person with a legal interest can file a request with the Commission to initiate the *ex post* control. After verifying the information in the request, the Commission shall adopt a decision based on this Law and inform the party that filed the request about it. (Article 17)

As envisaged by the Law, “[i]f, within the *ex post* control, the Commission finds any flaws, it shall fix a deadline within which the state aid grantor shall be under obligation to remedy such flaws. If the state aid grantor fails to remedy the flaws within the specified deadline and fails to inform the Commission about it in writing, within 5 days after the expiry of deadline referred...the Commission shall take the decision on unallowed state aid”. (Article 18) With this decision, the Commission also orders the State aid grantor to, without delay, take measures to recover the State aid amount that was granted, increased by the default interest prescribed by law, from the day of using such aid until the date of recovering the used amount. Pursuant to the same decision,

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<sup>41</sup> This has especially been advocated by Transparency Serbia in its report claiming that the Commission is *de facto* left without the power to inform on the intention of the grantor to grant the State aid, as well as in situations when the grantor does not want to provide information, leaving it as a “control state body in a dire situation”. (Transparency Serbia 2015, 4)

<sup>42</sup> There are indications that this has happened on several occasions.



the State aid grantor shall be ordered to immediately discontinue the further granting of the unused portion of State aid. The informants confirmed that no such decision has been made to date, raising some concerns about the ability of the Commission to cope with challenging cases.<sup>43</sup> The law envisages that the Supreme Audit Institution, the Republic's authority for budget inspections, and other relevant budgetary institutions on the regional and local level, should be informed about the decision. It also envisages that the government should be informed. (Article 19) This leaves the Commission with very little power to enforce the decision itself, but rather vests this responsibility in other parts of the Government and in an independent audit institution. This may be criticised, as it does not provide for an adequate accountability mechanism and leaves the Commission as a sort of "paper tiger" that is not able to fully scrutinise grantors' actions.

The Commission's decisions are final, but it is possible to challenge them in administrative court. An administrative dispute can also be initiated if the Commission does not adopt a decision within the period specified by the Law. It is also envisaged, that "[t]he lawsuit by which the administrative dispute was instigated shall not stay the execution of the Commission's decision". (Article 20) As attested by the informants, there have been only three challenges to date, all by competitors of State aid beneficiaries, and all unsuccessful.

The Law also provides mechanisms for resolving conflicts of interest, as members of the Commission are *de facto* representatives of the ministries that are the greatest State aid grantors. It is envisaged that they will respect the provisions of the law governing the prevention of conflicts of interest in the discharge of their public functions. "A member of the Commission who is at the same time a representative of the state aid grantor, or the proposer of the regulation constituting the grounds for state aid granting, may provide additional information within the state aid control procedure but shall not have the right to take part in the decision-making process." The informants confirm that this rule has been adhered to in the practice of the Commission, but it still remains that control is left in the "representatives" of the aid grantors that need to be controlled. In terms of the provision of information, a representative of the State aid grantor or the proposer of the regulation constituting the grounds for the granting of State aid who is not a member of the Commission shall be entitled to participate in the State aid control procedure to provide additional information, but shall not have the right to take part in the decision-making process. The

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<sup>43</sup> Transparency Serbia has especially pointed to this fact, i.e., that the Commission has not made a single decision for *unallowed aid* to be returned. For more comments on the Commission's practice, see: Transparency Serbia (2015).

Commission may also invite representatives of other authorities, organisations and professional associations to provide further information of relevance for decision making, but they shall not have the right to take part in the decision-making process. (Article 21)

Members of the Commission and persons employed by the Ministry of Finance are under an obligation, even after the termination of their mandates or employment, to maintain the confidentiality of information obtained within the State aid control procedure that the State aid grantor or beneficiary has designated as professional secrets.<sup>44</sup> Information is not to be disclosed or communicated to third persons without the explicit written consent of the person whom they concern, unless the competent authority is required by law to do so. (Article 22)

Finally, the Law contains reporting provisions. (Article 23) Based on the information collected from the State aid grantors, the Ministry (not the Commission) prepares the proposal for the annual report on the State aid granted in the Republic of Serbia, which the Commission submits only to the Government (but not the Parliament). The Ministry also specifies in more detail the methodology for the drafting of the annual report, the deadline for the submittal of data to the Ministry, and the deadline for the submittal of the proposal for the annual report. As confirmed by the informants, composing reports has proven to be a challenging task due to multiple factors which include the lack of administrative capacities (i.e. the lack of personnel within the ministry), the lack of response by the aid grantors, and in some cases, the absence of knowledge of the obligation to inform about the aid granted (although this has changed over the years).

In practice, a provision of article 25 has proven particularly challenging; it envisages that: “Within a period that cannot exceed one year as of the date of commencement of the application of this Law, the Government shall adopt a programme of compliance of state aid schemes and individual state aid with this Law, which are effective until that time and continue to be so after the date of commencement of the application of this Law.” This programme has still not been adopted by the government, and thus, an important obligation arising from the SAA has not yet been fulfilled. This has been stressed as a problem in the regular reports prepared annually by the European Commission on the progress of the candidate.

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<sup>44</sup> The confidentiality of information has proven to be an important part of the State aid regime in Serbia, as many of the investment agreements still remain secret to certain extent, especially those involving State aid.

### **3.2.1. Bylaws on the rules for State aid granting and procedures for State aid granting**

As was already pointed out, the substantive provisions on State aid control are set by the Regulation on the rules for State aid granting. This lengthy legal act has been amended several times so as to adhere to the changing content of the EU's State aid provisions, which have undergone significant changes over the past year in the context of the crisis and as a part of the modernisation package undertaken by the previous EU Commission.<sup>45</sup> The Regulation, in addition to the basic provisions, prescribes rules for 1) regional State aid (for investments, small and medium enterprises and for operations), 2) horizontal State aid, and 3) sectoral State aid (Steel Production Sector, Coal Extraction Sector, Transport Sector). The horizontal aid rules are divided into several categories according to the EU's substantive rules for: Small and Medium Enterprises, Rescuing and Restructuring Enterprises in Difficulties, Employment, Environmental Protection, Research, Development and Innovation, and the Cultural Sector.

Especially interesting for this analysis is employment aid, which is specifically envisaged for Employing Disadvantaged Workers, Disabled Workers, and State Aid for Compensating Additional Costs of Employing Disabled Workers. We are particularly pointing to this type of aid, as it has been used extensively by successive governments in order to attract investors over the observed period, but also prior to the entry into force of the State aid rules.

It is also important to stress that, to date, very few State aid measures have been reported or allowed by the Commission in the areas of research and development, and well as for environmental purposes.<sup>46</sup> That is not completely unexpected in the given political context, but it is still surprising, keeping in mind: a) the country's economic development aspirations, and b) the need to substantially change the protection of the environment.<sup>47</sup>

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<sup>45</sup> For modernisation in the period 2009-2014 see *inter alia*: Segura Catalán, Clayton (2013).

<sup>46</sup> See: Report on State aid (2012, 2013); Stojanovic, Radivojevic (2012, 359).

<sup>47</sup> The costs of implementing the EU environmental *acquis* are estimated at around 12 billion EUR. Therefore, substantial aid both for national public and EU funds will be required in the coming period. See further: National Environmental Approximation Strategy for Serbia (2011).

A special chapter of the Regulation is dedicated to *de minimis* aid. The threshold adopted is rather high for local standards, standing at RSD 23, 000,000<sup>48</sup>, just below the EU threshold of EUR 200,000. *De minimis* aid was the issue that proved to be challenging for the system in its first years. First, the Commission was overwhelmed with *de minimis* applications, leaving little room to concentrate on *ex officio* investigations and larger cases having a more significant impact on competition. That has been remedied by changes to the Regulation. The other challenge is connected to the first one and stems from the absence of a provision for relevant information on State aid from grantors to the Ministry which is in charge of keeping a central register on *de minimis* aid. This consequently triggers the problem of calculating the accumulation of aid and observing whether some enterprises and measures fall outside of the scope of the *de minimis* regime. Even without significant consequences on competition, this inconsistency in implementation might influence the competitiveness of small and medium enterprises, especially in the local context when granted aid on the basis of political decisions. Therefore, an improved regime would have to take this into account and devise mechanisms for keeping all of the measures under control and not letting them escape “under the radar”.

For developing State aid regimes, export aid, which is forbidden by rule, has proven to be especially challenging. However, it is possible to disguise this aid using other measures, primarily by aiding exporters through measures aimed at employment or through regional aid. Given the fact that the approach towards the granting of State aid has shifted in the EU itself with the European Commission expediently granting clearance for multibillion euro schemes<sup>49</sup> and having upheld the plans of several governments to aid the automotive industry in the given period, it is not surprising that the Serbian government has acted on the same note. It was effectively granting aid, or bailing out banks and promoting investments in sectors traditionally perceived as foundations of the industrial development in the country and in job makers with spill-over effects in other sectors of the economy. A similar example occurred in Poland, which had many challenges in the transformation of its economy, and the provision of State aid remained after its association.<sup>50</sup>

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<sup>48</sup> Around EUR 192,000 at the current exchange rate (2015).

<sup>49</sup> For the expedient procedure of State aid control in the EU during the crisis, see *inter alia*: Werner, Maier (2010).

<sup>50</sup> Paczkowska-Tomaszewska (2006, 669).

It has been pointed out by both the European Commission and the non-governmental sector that Serbian provisions are not fully in line with the *acquis*. This is, to some extent, the consequence of the ever-changing State aid regime in the EU itself. The problem was underlined by Schutterle: "Rather the substance of *acquis* needs to be incorporated in substantive national law. As far as codified EU law exists, that may not be too difficult. It is, however, impossible for any national legislature to transpose completely into national law all non/codified substantive State Aid *acquis* elements." (Schutterle 2002, 582) Indeed, the changing regime needs to be constantly followed and transposed by the eight members of the State aid department that are in charge of preparing proposals for Regulation change for the government in addition to their regular job of preparing State aid notification decisions, providing advice and education to the beneficiaries, and preparing State aid reports.

The Regulation on the rules and procedure for State aid notification<sup>51</sup> provides that the State aid grantor and/or the party proposing a regulation that serves as a basis for granting State aid shall submit State aid notification to the Commission for State Aid Control *before* State aid is granted, i.e. before the legislative act is sent for adoption. State aid notification is to be accompanied by the Standard Notification Form, and if necessary, the Supplementary Information Sheet. Upon request of the Commission, the Applicant shall submit other data and information in accordance with the Law on State Aid Control. This very brief document, containing only six articles, is accompanied by the Standard Notification Form and the Filing Instructions, which are an integral part of the bylaw. The Supplementary Information Sheet is published on the Commission's web presentation. Finally, this act envisages that State aid notifications are submitted to the Commission via the Ministry of Finance by post and by email, which is a consequence of the Commission having no seat and being served administratively only by the Ministry of Finance. As the insights gathered during the qualitative research and as the other report points out, the data provided to the Commission are limited in many cases, so there is still substantial room for improvement and for development in the practice of filing complete notifications to the Commission. This might, to some extent, be improved by better education of the applicants' employees and might be technically advanced through better information and more detailed information sheets. However, the basic challenge is beyond the technical side and is caused by the applicants' inactivity (not filing notifications in the worst cases) or their delayed filing of notifications once a scheme has already been adopted or even implemented. This leaves little

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<sup>51</sup> "Official Gazette of RS", no. 13/2010.

room for the Commission to remedy inconsistencies, as their disposable mechanisms are limited and inadequate.

### **3.3. Conditionality and European Commission reporting on the progress of the reforms**

Part of the conditionality approach is the regular monitoring and examining of the progress made by a candidate in implementing reforms and in its approximation to EU standards. In the 2014 report, a relatively negative overview of the State aid regime in Serbia was provided. It was put forward by the Commission that “[r]educing the heavy state influence in the economy requires tackling inefficiencies in the large public sector, advancing privatisation in line with the schedule, streamlining state aid, and improving corporate governance of public companies”. (European Commission 2014, 4)

Assessing the ability to take on the obligations of membership, it was underlined that: “There is also a lack of institutional coordination and leadership in some key *acquis* areas and the need to safeguard the independence of regulatory bodies. The legislation on state aid control must be aligned with the *acquis* and effectively applied to all undertakings, including those in the process of restructuring and privatisation.” As the report covers a range of areas, the Commission does not point to particular State aid provisions that need to be aligned with EU law. However, it was openly underlined that: “Further efforts are needed in particular in the area of state aid control, especially to ensure the operational independence of the Serbian Commission for State Aid Control and to repeal the exemption of enterprises under privatisation from state aid rules.” (European Commission 2014, 9)

Examining the State influence on competitiveness, the Commission has underlined that: “State-owned, monopolistic structures dominate many sectors and the state continued to subsidise them heavily. Since the beginning of 2014, until the end of July, government subsidies expenditure increased by a real 7.1%. Contrary to previous years, the annual State aid report for 2013 has been delayed and was not available by the time of writing this report. State aid control needs to be enforced consistently and the exemption from state aid rules given to enterprises that are being privatised still needs to be abolished. New state aid measures need to be systematically notified before being put into force. The Commission for State Aid Control still has to demonstrate its independence. Overall, the state continues to substantially and negatively influence

competitiveness by providing significant and wide-ranging forms of state aid. The system of state aid needs to be thoroughly reviewed.” (European Commission 2014, 22)

This warning report came after some rather harsh reports in 2013, pointing to very little progress being made in the area. In 2013, it was stressed by the Commission that: “Further efforts are needed in particular in the areas of state aid control, where the independence of the Commission for State Aid Control needs to be further established and the exemption of enterprises under privatisation from state aid rules need[s] to be repealed.” (European Commission 2013, 4) Examining that year, as well as the previous year, the Commission outlined that: “There was very little aid given to training and to research and development. Most of the aid was given in subsidies (close to 60%) or as tax incentives (32.6% of total). State-controlled, monopolistic structures remain in a large number of sectors and the state continued to subsidise heavily the transport sector, which received almost a fifth of all aid. State aid control needs to be enforced consistently and the exemption from state aid rules given to enterprises that are being privatised still needs to be abolished. New state aid measures need to be systematically notified before being put into force. The Commission for State Aid Control still has to demonstrate its independence through ex post controls and [the] use of the provision on [the] recovery of unlawful state aid. *Overall*, the state continues to substantially influence competitiveness by providing significant and wide-ranging forms of state aid.” (European Commission 2013, 20) “The CSAC needs to demonstrate its operational independence, particularly from state aid granting bodies. Further efforts are needed to ensure that aid measures are notified to the CSAC and approved before being granted.” (European Commission 2013, 25) The final remark is important, as it points out that “independence through ex post controls and [the] use of the provision on [the] recovery of unlawful state aid” might, in practice, be considered the substance of the standard of having an “independent operational body”. We will come back to these standards in part 3, where we analyse the position of the Commission.

This came after a relatively moderate report in 2012.<sup>52</sup> The 2012 report underlined: “There has been some progress in the area of State aid. A first comprehensive State aid report was adopted in September 2011. In addition, the government adopted the list of State aid schemes that need to be aligned with the *acquis*. A decree on the rules for granting State aid was amended

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<sup>52</sup> We have opted to present reports back to 2012, as the previous reports covered the period in which the Commission was making the first operational steps and the country, in general, had yet to fully introduce the system.

in December 2011 to broaden its scope to public enterprises. The number of notified State aid measures increased substantially, thanks to increased awareness among relevant State aid grantors at all levels of government. The Commission on State Aid Control (CSAC) took 148 decisions, including 78 conclusions in the *ex post* control procedure. Eight *ex post* control procedures were launched *ex officio*. However, further efforts are needed to make aid grantors notify their projects before State aid is disbursed and to ensure the timely alignment of existing State aid schemes. The Commission's enforcement record needs to be strengthened and its operational independence is still to be demonstrated. Cooperation and coordination needs to be stepped up between the CSAC and all bodies granting State aid. Concerning liberalisation of specific sectors, a number of Serbian undertakings continue to enjoy, *de facto* or *de jure*, special or exclusive rights, e.g. in the fields of energy, transport, infrastructure, postal services, telecommunication services, broadcasting, agriculture and the environment. Additional efforts need to be made towards market liberalisation in line with the *acquis*." (European Commission 2012, 35)

The detailed analysis of specific cases of State aid is outside of the scope of this paper. In a transitional context, the State aid measures dealt with by the Commission and included in the relevant annual reports mostly have included restructuring aids and investments in new production capacities in Serbia. It is without doubt that, in a transitional period, State aid is both required and expected by a number of sensitive sectors that are facing difficulties stemming from the transition and the opening of the market, on the one hand, and the consequences of the economic crisis, on the other. These sectors traditionally include the steel, mining and transport sectors.<sup>53</sup> However, in speaking about sensitive business sectors and underdeveloped regions in the new and prospective European member states, we must not disregard the limiting fact that one country's State aid issue might tomorrow become an EU-wide cohesion challenge, putting more and more pressure on richer nations within the Union to provide cohesion aid to the poorer ones. It is necessary to stress the political and economic consequences of fully aligning State aid schemes, especially those aimed at failing undertakings that are in a state of (never-ending) restructuring.

With or without (unlikely) temporary derogations for certain sectors, Schimmelfennig and Sedelmeier rightly argue: "In the end, however, rule adoption requires the authoritative decision

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<sup>53</sup> For Polish experiences in sensitive sectors, see: Bieganski (2008)



of the target government, which seeks to balance EU, domestic, and other international pressures in order to maximize its own political benefits. The most general proposition of the external incentives model under a strategy of reinforcement by reward is therefore that *a state adopts EU rules if the benefits of EU rewards exceed the domestic adoption costs.*" (Schimmelfennig and Sedelmeier 2004, 664) In the field of State aid and in light of enlargement fatigue and unpredictable membership prospects, the full implementation of a burdensome regime is not likely. This is especially the case for governments that are facing high expectations by their populations to achieve better living conditions (which the provision of State aid to companies inevitably does for limited, but sometimes vocal, groups). If the prospects of membership are not clear, and with election cycles always in sight in fragile, unstable democracies, it is unlikely that the government will make such sacrifices.

#### **4. Institutional challenges and obstacles**

In this part, we turn to one of our main research focuses - the institutional framework for State aid control in Serbia. As previously mentioned, the Serbian Government opted for a hybrid solution forming an independent commission entrusted with control tasks, but without a separate budget or administrative capacity for the work. This body was entrusted with controlling State aid measures until Serbia's prospective accession to the European Union, when this obligation will cease to exist and the power to scrutinise State aid measures will be transferred to the European Commission.<sup>54</sup> The Commission is itself a hybrid, a semi/governmental advisory body, rather than a watchdog. This is a legitimate policy approach, given the fact that the country is in a transitional period in which it is preparing to fully implement EU law. However, this approach has demonstrated some weaknesses that we point out in the analysis.

"The transformation of [the] Serbian administration has been influenced by two major intertwined processes. The first is the transformation to the modern market economy; the second is integration into the European Union. Due to the extent and pace of reforms implemented for accession to the European Union, the process of reforms is, in the public (both expert and general), often equated with the process of the country's integration in the EU. After the

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<sup>54</sup> For more on the possibilities for a decentralised State aid control in the EU context, see: Nikolaidis (2003).

disintegration of the Socialist Federal Republic of Yugoslavia, during the union with Montenegro, Serbia underwent a problematic and slow process of social and legal changes, including market reforms and a privatisation process, which took place in the midst of the regional wars and UN sanctions....With the fall of Milosevic's regime and [the] inclusion of Serbia in transnational integration processes, it was necessary to introduce a number of modern institutions able to facilitate economic, legal and societal change. Societal and political change in Serbia, alongside public agencies, incorporated the introduction of a number of independent regulatory and control bodies, which include the Ombudsperson, the Commissioner for access to public information and personal data protection, the Anti-discrimination commissioner, the Anti-monopoly commission, and the State audit institution, etc. These were new bodies for the Serbian political sphere; thus the start-up of their work was more than challenging, and it was necessary to negotiate many budgetary obstacles and the lack of political will (predominantly from the government's side) to enable the smooth enactment of activities. The challenges included finding appropriate office space, hiring qualified personnel and, later on, ensuring the implementation of decisions made by these bodies." (Milenkovic and Milenkovic 2013c, 136-137, 140) All of this is, to a great extent, applicable to State aid control as well.

Serbia's Association and Stabilisation agreement foresees the introduction of an "independent operational body" that is competent to scrutinise State aid measures and their compatibility with EU aligned substantive norms on State aid. However, the adopted Law on State aid control does not fully provide for an institution that might be considered to fulfil this criterion of "operational independence". The Commission has no legal personality, and no budget or separate administrative capacities, but rather, is served by the Ministry of Finance, which overwhelmingly hampers its proclaimed independence. Members of the Commission are *de facto* representatives of four relevant ministries, with one member from the Commission for Protection of Competition, appointed for a five-year period pursuant to the decision of the government. Research conducted over the previous period demonstrates that, from the onset, the position of the State Aid Control Commission in Serbia was ill-grounded. This institutional design, making the Commission overwhelmingly dependent on the Ministry of Finance and other State aid grantors, has evidently led to its weakness in acting as the independent body it was proclaimed to be.<sup>55</sup>

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<sup>55</sup> However, it is not surprising, but rather, is recognised as a trend in all of the countries in the region, see: Botta (2013).

We find the institutional aspects of the State aid reform to be crucial for this analysis. With a civil servant corps that is insufficient in number and in types of expertise, on the one hand, and the lack of functional independent bodies, on the other, it is unlikely that the country will be able to bring about legal change or implement such change. Therefore, the EU's insistence on the introduction of objective and impartial civil servants or control bodies that are able to examine and scrutinise State aid is a precondition for the success of the reforms.

By virtue of the Law (Article 6), the Commission has five members and is set up by the Government, and its members are elected by the Government upon the proposals of: the ministry responsible for finances; the ministry responsible for the economy and regional development; the ministry responsible for infrastructure; the ministry responsible for environmental protection; and the Commission for the Protection of Competition. The representative<sup>56</sup> of the ministry responsible for finances is, at the same time, the Chairperson of the Commission, and the representative of the Commission for the Protection of Competition is the Deputy Chairperson. The conditions for membership in the Commission are Serbian citizenship and "at least a university degree", and it is required that a member must "possess expert knowledge in the field of state aid, competition, and/or EU legislation." Thus, by broadly defining this criterion, it was actually enabled to appoint members without prior in-depth knowledge of State aid.<sup>57</sup> Members of the Commission are appointed for a period of five years and can be reappointed, based on the proposal of the same proposer. The mandate of the Commission member shall cease: 1) upon expiry of the period for which he/she is appointed; 2) if he/she acts contrary to the provisions of the Law; 3) if he/she does not respect the provisions of the Commission's Rules of Procedure; 4) if unconditionally sentenced to a prison term of at least six months; 5) at personal request, by submitting a letter of resignation.

Members of the Commission are remunerated for their engagement in the Commission, as determined by the Government. The Commission is charged with adopting its rules of procedure and is explicitly defined as "operationally independent". The Commission has no separate budget; rather, it is provided by the Law that funds for the activities of the Commission

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<sup>56</sup> "Representative" is the very formulation used in the Serbian original text, pointing to the approach taken by the Law to form a control body representative of the biggest aid grantors.

<sup>57</sup> Fifteen years after the commencement of the EU-led reforms, it is surprising that such a provision is still in place, given the fact that a sufficient number of experts is now available with a suitable level of knowledge about State aid.

shall be provided from the budget of the Republic of Serbia, and that the Ministry shall provide the premises and other technical requirements for the activities of the Commission. (Article 7)

The Commission competences are: 1) within *ex ante* control, to decide on whether notified State aid is allowed; 2) within *ex post* control, to decide on whether granted State aid is allowed; 3) to make decisions and conclusions on the procedure of *ex ante* or *ex post* control; 4) to submit to the Government an annual report on State aid granted in the Republic of Serbia; 5) in performance of its responsibilities, to cooperate with the Supreme Audit Institution, the Republic authority for budget inspection, the autonomous province department, namely, the department of the local self-government unit responsible for budget inspection, and with other domestic and international authorities, organisations and institutions; 6) to publish, on its internet page, decisions that it adopts in the procedure of *ex ante* and *ex post* control, the annual report on State aid granted in the Republic of Serbia after it has been adopted by the Government, as well as other data and information that it deems to be relevant to the application of this Law; and 7) to perform other tasks in accordance with this Law. However, the very next article makes this concept of operational independence questionable, in a practical sense, as it envisages that all “Specialist, Administrative and Technical Activities” of the Commission will be carried out by the Ministry of Finance. These include: 1) collecting and processing the notifications and other data about State aid; 2) preparing the decisions of the Commission in the procedures of *ex ante* and *ex post* control; 3) keeping records regarding State aid; 4) preparing the proposal for the annual report on the State aid granted in the Republic of Serbia to be submitted by the Commission to the Government; 5) cooperating with the Supreme Audit Institution, the Republic authority for budget inspection, the autonomous province department, namely, the department of the local self-government unit responsible for budget inspection, and with other domestic and international authorities, organisations and institutions in the field of State aid control. In addition to the above-mentioned tasks, the Ministry also performs the tasks of preparing the legal acts regulating State aid control, as well as the proposals for amendments thereto, and other tasks in accordance with this Law. Gjevori points to similar problems faced by the Albanian State Aid Commission, questioning this concept of “independence within government”. (Gjevori 2014, 18)<sup>58</sup> She points to criticism by the European Commission regarding the operational independence of the Albanian

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<sup>58</sup> See this chapter for an overview of the introduction of State aid in Albania.

Commission in practice; very similar problems may be observed elsewhere in the region. (Botta 2013)

A comparative analysis of former candidates points to several possible modalities of organising the State aid control in terms of the institutional setting. The first is to entrust this competence to a body within the Ministry of Finance or closely connected to it, and in some cases, these competences have been entrusted to bodies charged with monitoring competition within the country.<sup>59</sup> Atanasiu indicates that finding an adequate position of the bodies entrusted with State aid control is a challenging task, with the dilemma of whether it is better for them to be independent agencies or government bodies with the advantage of being close to the state structures that are aid grantors. She also points out that the relation of the control body and the state structures creates complex legal, political and even constitutional problems. (Atanasiu 2001, 262) Indeed, this is a challenging question with no easy answer.

It is important to note that most of the aforementioned bodies withheld some competences after the accession of their countries to the EU in 2004 and 2007. Since, from the day of a country's accession, the European Commission is formally solely in charge of clearing State aid measures, these bodies have been transformed into valuable national reference points for grantors. They are usually entrusted with pre/notification checks of the compatibility of State aid measures, the provision of advice to grantors and even with checking the compatibility of *de minimis* measures and those covered by the General Block Exemption regulation. As these represent a vast number of measures, the new role is very significant. Most of the bodies are also entrusted with preparing the report on State aid measures in the country. Therefore, it is expected that a State Aid Commission in Serbia (or a different body, given the task) will be similarly entrusted with these competences.

The above-explained Serbian model may be even characterised as the control of State aid by the Ministry of Finance, with some elements meeting the standard of an "independent operational body". The budgetary independence of the Commission, or rather, the lack of it in this case, is very important for the overall position of the control body. Having no separate budget or resources to finance its activities, the Commission is completely dependent on the Ministry of Finance. In practice, it has proven to be a functional model, but with many shortcomings. However, in addition to the lack of administrative capacities, it is necessary to point out that the

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<sup>59</sup> Atanasiu (2001, 263); Schutterle (2002, 579), Botta (2013).

Commission's members are remunerated for their work directly from the budget and in the amount of 1.5 times the average salary in Serbia. Given the fact that the average salary in Serbia is relatively low and that the members are envisaged to be selected on the basis of their expertise in the fields of State aid, competition law and/or European Law, it is not possible to have members who are dedicated to the job full time. Most of them are either working in their respective ministries (or the Commission for Protection of Competition) or in another post. That leaves them with limited time to handle cases and examine the details of the challenging legal and economic problems of State aid measures, i.e. to engage in delicate decision-making beyond the draft decisions prepared by the administrative service of the Ministry of Finance (whose eight staff members are already faced with a challenge in handling the workload).

Given the fact that the Government is facing budgetary burdens, it is unlikely that there will be a Commission for State Aid control that is an independent body with a separate administrative and technical staff working on these particular issues. However, neither is it viable to maintain the status quo, as it seems that the Commission has, to a great extent, reached its functional limits under these circumstances. It is, however, most viable to transfer the Commission's competences to the Commission for Protection of Competition, which would then be capable of having a separate department to work on these issues. As the Commission for Protection of Competition is independent in budgetary terms (as it collects its revenue from merger control fees and even pays some of the unspent funds into the central state budget), this would be the most suitable solution, both in terms of the necessary institutional independence and the financial resources needed to fund such administrative activity. Keeping in mind that the administrative capacities are very limited in this area, the transfer of those currently employed in these tasks in the Ministry to the Commission seems to be a viable solution as well.

## **5. Conclusions – finding an appropriate regime in the context of enlargement fatigue**

It is without doubt that the State aid regime in Serbia is a direct consequence of the EU's influence and is a prime example of conditionality being put into practice. It is necessary to distinguish between different types of conditionality, namely, those relating to the adoption of the *acquis* (which is far more measurable), and the political conditionality that is prone to discretionary measurement, such as the achievement of functional political institutions. In that regard, the introduction of a State aid regime and the alignment of aid schemes seem to be much more measurable and verifiable compared to other reform efforts. On the other hand, this makes all of the flows of the system harder to conceive so as to be regarded as an accountable partner that is ready to join the Community. Even in the absence of membership prospects, there is value in introducing this system into the economies in the region, including that of Serbia. This has also been reaffirmed by the intention of Serbian legislation. The Law has a dual goal - aligning with the rules of the EU and meeting international obligations, but also protecting competitors in the national market.

In addition to the legacy of planned economies, it is important to note that countries in the process of integration to the European Union largely have low living standards, and when State aid is considered from the perspective of aiding failing companies that are the only source of income for families in remote areas of the countries, analyses of the issue take on a different tone. Each analysis of State aid must therefore factor in these burdens when judging the (relative) success of the State aid reforms in Serbia and other Western Balkan countries.

It is without doubt that, in a transitional period, State aid is both required and expected by a number of sensitive sectors facing difficulties stemming from the transition and the opening of the market, on the one hand, and the consequences of the economic crisis, on the other. These sectors have traditionally included the steel, mining and transport sectors. However, in speaking about sensitive business sectors and poor regions of the new and prospective European member states, we must not disregard the fact that one country's State aid issue might tomorrow become an EU-wide cohesion challenge, putting more and more pressure on richer nations within the Union to provide cohesion aid to the poorer ones. It is necessary to stress the political and economic consequences of fully aligning the State aid schemes, especially those aimed at failing undertakings that are in a state of (never-ending) restructuring. The extent to which EU (including

the individual MS) conditionality will be “state aid conditionality” in the coming years has yet to be ascertained.

Given the fact that the Serbian government is facing budgetary burdens, it is unlikely to have a Commission for State Aid Control that is an independent watchdog with a separate administrative and technical staff working on these particular issues. It would, however, be possible to have the Commission’s competences transferred to the Commission for Protection of Competition, which would then be able to have a separate department working on these issues. As the Commission for Protection of Competition is independent in budgetary terms (as it collects its revenue from merger control fees), it would be the most suitable solution, both in terms of the necessary institutional independence and the financial resources needed to fund such administrative activity.

Since 2000, Serbia has come a long way in making political, legal and economic reforms. This period has been characterised by relative political instability and many international challenges for the weak democracy. Therefore, it is possible to say that the level of State aid control that has been achieved should not be considered unsatisfactory, even though much remains to be done. The implementation of the regime has drawn critique, as it has been stressed that the results to date have been more in line with meeting international obligations, rather than protecting competition. Although these are both proclaimed to be priorities of the law introduced, it should be stressed that State aid control is, after all, a very European specificity of market competition protection and does not exist outside of the context of the EU and the EU integration process.<sup>60</sup> In the context of the economic crisis and the constant search for the appropriate mechanisms to alleviate its consequences and to improve economic performance, it is not at all unexpected that successive governments have worked on meeting (most) of the obligations towards the EU, but have not made extra efforts in bringing a new competitive realm into the transitional market. Given all of the pitfalls of the institutional design, but also the relatively strong formal powers, it is easy to conclude that the Commission might have gone further in enforcing the regime. The question of how successful it could have been remains open to further interpretation given the fact that the implementation of this kind of control has, as its prerequisite, a change in the political culture in the country. It is a long process requiring time and gradual restraint on the part of the political decision makers having access to public funds. This process is not an easy one, even in the much more developed political systems in Western Europe. As it

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<sup>60</sup> Save for WTO rules on subsidies.



was invoked earlier in the paper, it is a question of whether the (political) cost of domestic adaptation is lower than the possible gains that might be achieved, in this case, the possible membership. A further challenge is the need for a change in the attitudes of competitors in the Serbian market. It will also take time for undertakings (both private and those still connected to the state) to depart from the policy of shopping for State aid, and move toward seeking protection and using the possible legal remedies (however limited at this point) so as to better enforce the regime and protect competition.

Finally, the EU faces another problem in the conditionality approach, which is vested in the very nature of the “reward” that may be offered to potential candidates. In addition to the visa-free regime, the pre-accession aid (limited in amount and effect) and trade liberalisation, there is little less else that the EU may offer except full membership. Countries in the region have already received all of these rewards and have free trade regimes guaranteed by international agreements with the EU and the member states. Although the success of the first phase of the implementation of the State aid regime in Serbia is not without doubt, the very insistence of the EU on introducing it at such an early stage provides room for the Serbian government to align the regime fully in the coming years prior to accession. In this twist of fate, enlargement fatigue plays a positive role, as it allows for more room to manoeuvre. However, without a clear membership prospect, it is highly unlikely that any government will abolish its widely-used schemes (which fall outside of the rules).

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