

Transformation of Public Utility Companies in the Republic of Serbia

European Agency for Reconstruction
(EAR) in Belgrade

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Municipal Infrastructure Agency Support Programme

An EU-funded project managed by the European Agency for Reconstruction

9R5927/CvS/R2006_97/R001

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Report



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EXECUTIVE SUMMARY

INTRODUCTION

Under the EAR sponsored Municipal Infrastructure Agency Support Programme (MIASP), the Consortium, consisting of Royal Haskoning, The Institute for Housing Studies (IHS) and Deloitte assists the European Agency for Reconstruction (EAR) and the Municipal Infrastructure Agency (MIA) in preparing technical and financial project documentation for municipal infrastructure projects and in the monitoring of implementation of those projects¹. The purpose of the programme is to enable municipalities and local public utility companies in the Republic of Serbia to access financial resources for feasible infrastructure projects.

One of the objectives of the MIASP is to enhance the capacity of Municipalities and Public Utility Companies (PUC's) in order to ensure the proper implementation and the sustainable operation of project investments. This programme component consists of three parts, as follows:

- to organise various training programs on project preparation, project implementation and municipal infrastructure planning and finance;
- to assess the performance of PUC's that are directly involved in the program and prepare Capacity Enhancement programs to ensure the adequate operation and maintenance of project investments;
- To assess relevant developments in the water supply and wastewater, district heating and solid waste sectors in Serbia and to propose strategies to transform Public Utility Companies responsible for Municipal Infrastructure into efficient and service oriented corporations"

This report presents the results of the activity mentioned under the third bullet above.

ASSESSMENT

An assessment has been made of relevant developments for PUC's in the water supply and waste water sector, the district heating sector and the solid waste sector in Serbia. These sectors were selected because they covered most of the municipal infrastructure projects under the MIASP. In all three sectors the following aspects have been reviewed:

- Sector policies
- Regulatory framework
- Sector operations through municipalities and Public Utility Companies.

The above aspects have been reviewed with a focus on their impact on the performance and functioning of PUC's in the relevant sectors.

¹ Inception Report - Municipal Infrastructure Agency Support Programme - Additional Services Republic of Serbia, European Agency for Reconstruction in Belgrade, May 2006.





CONCLUSIONS ON SECTOR POLICIES

Sector policies are characterized by the following issues:

- Ambitious targets to overcome the backlog in investments
- A drive for harmonization with EU legislation, regulations and directives;
- A drive for regional approaches, such as
 - regional solid waste schemes and
 - Water basin approaches
- A trend towards guided and voluntary association of local self-governments
- Directions for improved performance and efficiency of PUC's, including:
 - Reduce Unaccounted for Water
 - Increased energy efficiency (district heating)
- A drive for achieving full cost recovery based on the polluter/user pays principle

CONCLUSIONS ON THE REGULATORY FRAMEWORK

The assessment of the regulatory framework is summarized as follows:

- PUC's are established by municipalities and are operating under public law
- Legal ownership of assets of municipalities rests with the National Government
- Public administration reform policies assume transfer of more responsibilities to municipalities
- Sector regulation and enforcement are still weakly developed
- National (financial) policies limit tariff levels for public utilities
- No systematic monitoring and/or benchmarking takes place of PUC's at sector level

CONCLUSIONS ON SECTOR OPERATIONS

- The small average size of PUC's results in a lack of professional capacity to efficiently manage and develop their operations;
- Assets of PUC's are formally owned by the National Government which limits possibilities to manage these assets in an optimal way and e.g. use assets as collateral to obtain loans.
- PUC's operate with tariffs that in most cases only recover the costs of operation and maintenance. Generally speaking tariffs are too low and PUC's have become financially dependent on the municipalities that own them. The National Government in certain years limits tariff increases to certain levels in order to control inflation.
- In many PUC's management operates as part of the municipal administration and as such they have become subject to (political) interference limiting possibilities for professional management; in some Municipalities the top management of the PUC is replaced when a new mayor is appointed.
- Having become part of and fully dependent on government bureaucracy and without adequate revenues it has become very difficult for PUC's to develop and implement strategic and long term development plans.
- Low salary levels and limited professional challenge make it difficult for PUC's to recruit capable professional staff.





- Many PUC's have become part of a municipal bureaucracy, which makes them organisations with an administrative and technical drive that are less sensitive to customers' demands.
- Due to a lack of investments and resources PUC's experience difficulties in operations and maintenance resulting in low efficiencies and inadequate service levels.
- Many PUC's in all sectors share a lack of professional management and support systems and their size is too small to have access to financial resources to make the necessary investments.

IMPROVING INSTITUTIONAL EFFECTIVENESS OF PUC'S

In order to improve the level of service delivery a transformation of public utility companies is needed along the following lines:

- Enlargement and Up Scaling of PUC's beyond municipal boundaries through regionalization will allow PUC's to professionalize and improve their services and increase efficiency by making use of economies of scale.
- Corporatization of PUC's, creating a more businesslike relationship between PUC management and their owners, allowing PUC management to concentrate on the development of a professional and service oriented organisation and simultaneously allowing shareholders to extend sufficient direction and control.
- Strengthen the financial position of PUC's by allowing PUC's to set adequate tariffs for high quality services and gradually achieve full recovery of operational and capital costs and to make optimal use of assets for the further development of their organizations.

In order to realize the above, measures are needed at the sector level as well as the municipal and PUC level. Sector policies, laws and regulations and investment programs need to be designed in such a way that these provide direction and enable the desired transformation of PUC's at the municipal and regional level. Below a summary is given of the main measures that need to be taken:

- Further develop sector policies and strategies stimulating inter-municipal and regional approaches, especially for the water & wastewater sector and for district heating.
- Develop sector investment programs in support of regional and inter-municipal approaches and discourage investments that lead to sub-optimalisation
- Develop legislative and organisational models for inter-municipal cooperation and create the legal possibilities for public utilities to operate on a more commercial basis (e.g. under commercial law),
- Stimulate the use of Service Level Agreements and/or Concession Contracts to specify the expected service levels for public services and the resources to be made available to achieve them.
- Organize benchmarking of PUC's per sector in order stimulate and allow for monitoring of PUC performance
- Restrain interference from the national level to limit tariff increases for public utilities as long as these do not achieve full cost recovery
- Arrange for the transfer of assets from national level to local government level
- Establish and strengthen regulatory agencies in each sector to monitor and if necessary regulate service levels and related tariffs
- Strengthen enforcement of sector standards and regulations.





In the following sections the above measures will be discussed in more detail.

ENLARGEMENT AND UP SCALING OF PUC'S BEYOND MUNICIPAL BORDERS

Rationale for Up Scaling

Sector policies stimulate the development of municipal infrastructure services beyond the level of single (smaller) municipalities. The National Solid Waste Management Strategy outlines approaches for regional landfills to serve at least 200.000 people and to be owned and operated by more than one municipality. In the field of Water and Wastewater there is a tendency for planning and management at the water basin level and several regional projects are under preparation or underway. In the district heating sector there is a drive for increasing energy efficiency and to optimize the use of scarce energy resources. This implies that in ever more projects municipalities have to work together in delivering municipal services. The rationale for inter municipal collaboration is as follows:

Water supply and waste water sector

- river basin management as derived from EU Water Directives, and/or
- economies of scale

District heating Sector

- Larger urban centres serve surrounding municipalities
- Increase energy efficiency and use of energy resources
- Economies of scale

Solid Waste Sector

- The National Solid Waste Strategy provides the framework for regional solid waste schemes
- Rationale differs per activity (landfills, transfer stations, incinerators, etc.)
- Economies of scale

Stimulating Inter Municipal Collaboration

An important constraint for Inter Municipal Collaboration is the lack of awareness at the municipal and PUC level of the potential impact of this development (economies of scale, professionalisation and modernisation) in combination with a reluctance to give up direct (political) influence and control and a natural resistance to change. Therefore a number of “sticks and carrots” are necessary to stimulate inter municipal collaboration. Possible instruments include:

- Develop clear sector policies that provide direction for regional approaches
- Focus sector investment programs on regional projects and make inter municipal collaboration conditional for financial support
- Produce benchmarking results demonstrating the economies of scale of larger enterprises
- Intensify enforcement of technical and quality standards (e.g. closure of landfills that do not meet environmental criteria or enforcing waste water treatment if water quality standards are not met)





Institutional Aspects of Inter Municipal Collaboration

From the assessment of the various sectors it becomes clear that inter-municipal cooperation in the current situation is a relatively new phenomenon and not an easy issue, as municipalities are used to have direct influence on the PUC's in their area and are not likely to give up political control over these institutions.

In new projects, (draft) cooperation agreements are being developed that, for the time being, have to be based on current laws and must be in line with responsibilities of local self-government units and current rules regarding PUC management. This results in solutions in which all municipalities are closely involved in the establishment of the new institutions and in more important decisions and that in this way each municipality can block progress if certain solutions are not in line with their individual interest. Also in a number of cases old PUC's continue to exist and collaborate with the newly established regional PUC's, which may hamper effectiveness and limit efficiency gains.

From the above it appears that there is a need to develop various legal and organisational models for inter-municipal collaboration. Based on such models the Cooperation Agreement can be tailor made to the specific requirements of the municipalities and project concerned.

Corporatisation of public utilities can provide the legal and organisational framework for newly established regional public entities and also provide a clear management structure and more rational basis of involvement of the owners and users of municipalities involved.

CORPORATIZATION

The framework for analysing the process of Corporatization of PUC's is systematically presented in figure 1 below. The framework indicates the possible transition of ownership, rule of law and the legal status of organisation.

Figure 1: Framework for Corporatization

Ownership	Public Ownership		Private Ownership		
	Public Law		Private Law		
Rule of Law	Public Law		Private Law		
Legal Status	Public Administration	Public Utility	Public Enterprise	Private Company	Industry player Global brand

The above framework is used in the elaboration of the impact of a change in legal position on the management, operations and financial performance of public utility companies. Corporatization entails a change for PUC's from Public Utility into Public Enterprises that still have public ownership, but operate more independently under private or commercial Law. The purpose is to create enterprises that are service oriented with a focus on efficiency, which base their operations on Strategic Plans that are approved by the stakeholders and that are allowed to generate the resources necessary to implement these plans. Commercial Law enables the public stakeholders to exercise sufficient control through instruments such as annual reports and financial audits carried out by external auditors.





A strategy for corporatization consists of several elements. Recommendations with regard to some of these elements include:

- **Ownership of public enterprises:** In the long-term vision the municipalities remain shareholders and the real owners of regional public enterprises. The shares of individual municipalities have to be substantial in order to provide the perception of ownership and municipal investments. Increasingly private sector operators may be involved and may also provide part of the necessary investments in the infrastructure of the sector and contributing to improvement of management and operations.
- **Legal forms of corporate entities:** a form of Limited Liability Company seems more appropriate for regional enterprises, especially if assuming municipal ownership of the companies. In the future in some sectors (e.g. solid waste and district heating) joint stock companies may be established enabling utilities to open up to private sector involvement with major stakes in capital and management.
- **Public-Private Partnership / Private Sector Participation:** some forms of PPP / PSP will be present in the future, including Lease and Management Contracts and BOT and Turn Key approaches in infrastructure development. Already private sector operators have become active in the solid waste market and more developments in this direction are expected in the not too distant future.

While maintaining public ownership corporatisation will transform public utilities into public enterprises. The main advantages of Corporatisation of utilities are that it will transform public utilities into legal entities that will operate as enterprises with a more profound drive towards increasing efficiency and effectiveness, more open to consolidation of the sector and better positioned to attract private sector management and capital. The main legal forms in the corporatization process will be either to set up a Joint Stock Company or a Limited Liability Company, depending on the need to access private sector involvement will be needed in the near future.

STRENGTHENING OF THE FINANCIAL POSITION OF PUC'S

Many PUC's in Serbia are financially weak and do not recover their costs. Reasons for this are:

- Tariffs for municipal services in many PUC's only cover the cost of operation and maintenance. The cost of replacement of assets and for investments in system development are mostly not covered by the tariff (this is partly caused by the fact that in the past municipalities only had responsibility for operation and maintenance because ownership of assets lies with the National Government. Therefore traditionally tariffs were set to cover O&M costs only).
- Pricing of public services is often not based on real cost, but on political considerations. The economic decline during the past years has caused a reduction in income and therefore municipalities have been reluctant to increase tariffs of municipal services.
- Low efficiencies in operation of the systems cause higher costs than necessary;
- Low collection efficiency of bills n(e.g. for water the collection efficiency varies in most PUC's between 60-80%);





- In certain years the national government puts a limit on the tariff increase it allows in order to curb inflation. The maximum tariff increase that can be applied by PUC's in 2006 is 9.3%, which is below real inflation.
- Municipal budgets are limited and therefore subsidies from Municipalities are insufficient to fully recover the total costs of services.

Due to the above reasons, PUC's are not able to realize the necessary replacement of old assets and also not able to further develop their systems and related services. In order to improve this situation it is recommended to:

1. Allow PUC's to gradually increase tariffs for municipal services that fully recover the long term fixed and variable costs;
2. Improve the operational efficiency of PUC's by providing support to operational and financial performance improvement programs (see box below).
3. Stimulate benchmarking to be used as an incentive to promote efficiency improvement.
4. Transfer the assets of PUC's to municipal governments in order to enable the optimal use of these assets also for the further development of the systems and services;
5. Restrain interference from the national level to limit tariff increases for public utilities as long as these do not achieve full cost recovery

Financial and Operational Performance Improvement Planning (FOPIP)

Under MIASP it is proposed to carry out assessments and prepare and implement tailor made action programs for the individual PUC's in those Municipalities that have projects under implementation. In these programs emphasis will lie on the financial performance of PUC's but also other fields of activities (e.g. technical performance, organization or customer relations) may be included. A major issue will be an analysis of the tariff levels for municipal services and to develop together with the PUC's scenarios to adapt tariffs to the required levels. The following steps will be carried out:

1. Collect data and indicators of PUC performance and verify with the PUC that these data are correct;
2. Together with selected staff of the PUC assess the major problems and potential bottlenecks that may disrupt or hamper the implementation or sustainability of the project or the repayment of project loans;
3. Analyze together with PUC staff the causes of the identified problems and bottlenecks and formulate remedial actions;
4. Formulate and agree on an Action Plan that specifies the remedial actions to be undertaken by the PUC and/or the municipality and the activities in which the MIASP will provide technical assistance;
5. Implement the action plan in which the PUC will have the lead.

BENCHMARKING OF PUBLIC UTILITIES

One of the main challenges which could have great impact on institutional strengthening is development and implementation of benchmarking. From consultant reports it is clear that many PUC's still struggle with the collection and maintenance of relevant data of their operations. Either specific data are not available or the definition and quality of the data needs to be further addressed.





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Conclusions:

- Benchmarking can play a major role in the set up and monitoring of improvement projects.
- Per sector the elaboration of methods and systems may be quite different and must be further developed.
- The SCTM could act as a platform to organize such databases for the longer term with support of all municipalities or at first selected municipalities which show “best practice”.
- Support is needed from sector organisations and consultants that can be involved in the development of benchmarking strategies and in the design, development and implementation of related benchmarking systems and databases.





1 INTRODUCTION

1.1 Background MIA project

Under the EAR sponsored Municipal Infrastructure Agency Support Programme, the Consortium, consisting of Royal Haskoning, IHS and Deloitte, assists the European Agency for Reconstruction (EAR), the Municipal Infrastructure Agency and Municipalities in preparing technical and financial project documentation and in the monitoring of implementation of municipal infrastructure projects². The purpose of this programme is to enable municipalities and local public utility companies in the Republic of Serbia to access financial resources for creditworthy infrastructure projects.

One of the tasks of the MIASP is to assist the Government of Serbia (GoS) and EAR in formulating strategies to transform Public Utility Companies responsible for Municipal Infrastructure into efficient and service oriented companies and identify strategies and approaches to transform Public Utility Companies into viable and sustainable organizations that are able to meet a real demand for public utility services in a cost effective manner.

Due to economic decline and political developments in the last decade, Municipalities and PUC's have been unable to make the necessary capital investments and lack funds for proper operation and maintenance. The result has been a deterioration in service levels and a growing dependency on the municipalities that own them. In order to overcome these problems capital investments are needed and PUC's will need to increase revenues in order to generate sufficient income for adequate operation and maintenance and to service the loans needed to make these investments. A strategy needs to be formulated and legal, institutional and financial instruments need to be developed to transform PUC's into viable and sustainable organizations able to provide required service levels in a sustainable way.

In order to formulate this strategy, the MIASP team assigned Mr. Hans Kok, senior consultant on Utility Management of Royal Haskoning to undertake the following activities:.

- Have discussions with the Management of MIA and with the EAR Program Manager on the scope and purpose of the Mission;
- Have interviews with related Ministries (together with selected MIA/SP staff as required) on current policies and strategies with regard to the position and functioning of public utilities in Serbia;
- Interview senior municipal and PUC staff in selected Municipalities (together with selected MIA/SP staff as required);
- Review available information on PUC's in Serbia (a.o. from MIA Database)
- Review available legal and regulatory information from other relevant organizations or institutions;

² Inception Report - Municipal Infrastructure Agency Support Programme - Additional Services
Republic of Serbia, European Agency for Reconstruction in Belgrade, May 2006.





- Review options for the allocation of key responsibilities for municipal service delivery;
- Review options for the further Corporatisation and/or private sector involvement in the municipal services sector;
- Describe organizational and managerial 'best practices' in relevant PUC's;
- Propose an outline of MIA Guidelines for Transformation;
- Propose further activities necessary to complete the Guidelines.

1.2 Objectives

1.2.1. Main objective of the mission

The main objective of the current mission is³to assist the Government of Serbia (GoS) and European Agency for reconstruction (EAR) in formulating strategies to transform Public Utility Companies responsible for Municipal Infrastructure into efficient and service oriented corporations”

A “spin off” of the project could be the identification of projects for improvement of the transformation process of PUC's in the relevant utilities in Serbia to be funded by EAR.

1.3 Approach

1.3.1. Activities undertaken

The analysis of the PUC's in the target areas for water supply, waste water, district heating and solid waste will be based on:

- Interviews with relevant institutions;
- Interviews with donor organisations and funding agencies having experiences in public utility projects in the country;
- Analysis of relevant laws and regulations for the target sectors;
- Analysis of relevant reports of policies and projects in these areas;
- Inputs received from the MIASP team and information contained in the MIA database.

1.3.2 Planning of the activity

The planning of the activity has been as follows:

June 2006:

- fact finding mission (about 3 weeks)
- carry out problem analysis of the current situation
- identify missing information and ways to obtain this information
- identify bottle necks and constraints
- formulate options for transformation of PUC's
- debriefing with EAR and MIA

³ Terms of Reference Missions Hans Kok, June 2006.





July-August 2006

- collect additional information and
- collect missing data

September - October 2006

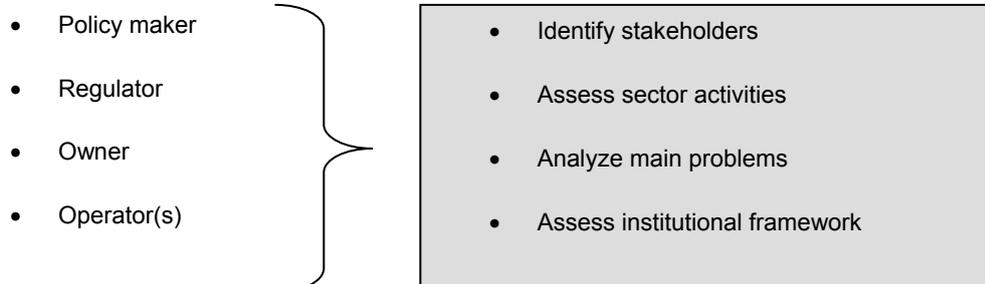
- second mission of Hans Kok (2-3 weeks)
- discussions with main stakeholders about various options
- prepare draft Report on Transformation of PUC's
- distribute draft Report for comments

November - December 2006

- third mission Hans Kok (1 week)
- finalize Report
- Presentation to stakeholders in Round Table Meeting in Belgrade

1.3.3. Analysis based on different institutional roles in sector management.

As for the sector problem analysis we have made a distinction between key roles and role sets in sector management such as the role of the policy-maker, the role of the sector regulator, the role of the owner and the role of the operator(s), as follows:



The framework for analysis has been applied to the sectors which are the most relevant to MIASP, being:

- The water supply and waste water sector
- The district heating sector
- The Solid Waste sector





2 ASSESSMENT OF THE RELEVANT SECTORS IN SERBIA

2.1 The Water supply and Waste Water Sector

2.1.1. Current Status

Water resources

The water resources in Serbia are generated for 8 % from available surface water within the territory of Serbia, while 92 % is taken from transit waters entering Serbia through the Danube, Sava, Tisa, Drina and other rivers. Groundwater resources are of special significance for the country as they provide up to 90 % of water supply for households and industry and about 70 % of the drinking water⁴.

Waste Water

Untreated industrial and municipal wastewater, agricultural run-off, as well as pollution related to river navigation and thermal power stations are the key sources of water pollution in Serbia.

Water quality

Quality of waters in Serbia is generally low and it is further deteriorating. Considerable contamination of water courses is caused by industrial and municipal waste water. It is estimated that 30 % of drinking water supply does not meet physical, chemical and bacteriological standards (67% in Vojvodina).

Water Supply Coverage

Based on the information included in the 2004 Statistical yearbook of the Republic of Serbia, the number of households being served by the public water supply system was 1.820.044 (5.460.132 inhabitants) out of 2.521.190 (7.563.570 inhabitants) households in Serbia and Vojvodina, meaning that around 72% of the population is served by means of a public water supply system.

According to a recent survey⁵ the following results were found (results from 109 out of 147 municipalities):

- Drinking water comes from groundwater, spring and surface water sources. About 59 % is from groundwater, 17 % from spring water and 24 % from surface water. In total, about 27 m³/s is extracted for public drinking water supply.
- The public water supply provides about 30 % of the capacity to industries according to the following table. The difference between produced and sold potable water results from losses (unaccounted water).
- The average amount of water losses is about 30 % according to the survey. However, 28 % of the evaluated municipalities reported losses of more than 30 % up to 50 %. The share of the total losses in all municipalities is 42 % for those mentioned before. Only 11 % of the municipalities estimated less than 10 % of water losses. Most of the municipalities have water losses between

⁴ Water Resources Development Master Plan, Information from Ministry, Directorate of Water, Serbia 2001.

⁵ Global Serbian Wastewater Study, EAR - 2005





20 % and 30 %, which is 54 % of the total water losses in the survey, mostly affected by the City of Belgrade with water losses of 34 % of the total losses.

- About half of the population receives water from the three largest water supply systems (Belgrade, Novi Sad and Nis), with the remainder served by medium-sized public water supply systems. About 76 % of the population has access to a public drinking water supply.
- Water supply in big cities is well developed. More than 90 % of the population is connected to the public water supply system in 23 % of the investigated municipalities. 45 % of the total population of Serbia live in these settlements.
- The coverage index is below 50 % in 25 % of the municipalities with a total of 13 % of the Serbian population. This mostly includes municipalities with 5.000 – 50.000 inhabitants.

2.1.2 Policy framework

An important and recent policy document concerning water resources and water quality is **The National Environmental Strategy** of the Republic of Serbia⁶, prepared by the Directorate for Environmental Protection of the Ministry of Science and Environment and published in June 2005. The Policy paper combines attention for different sectors (water and water resources, air and climate change, nature and biodiversity, forest and soil) into an integrated environmental strategy. The policy paper contains an extensive analysis of main problems in the different areas. From this Policy document we refer mainly to developments relevant for the municipalities in the country.

The Policy Paper gives much attention to non-sector specific causes for environmental degradation, such as:

- Poor integration of environmental policies with economic and other sectoral policies;
- Insufficient institutional capacity;
- Ineffective systems of monitoring and reporting;
- Inefficient environmental enforcement;
- Ineffective system of environmental financing and lack of economic incentives;
- Law on environmental awareness, insufficient environmental education and inadequate public participation in decision-making.

Many of these problems have to do with the municipalities as these are responsible for water supply and waste water on their territory.

Other Water related Policy Documents

One of the main documents concerning water sector policies from the responsible sector Ministry is the **Republic of Serbia Master Plan for Water**,⁷ which defines main water resources in the country and allocation to certain areas with less water resources. The Law on Design and Construction (OGRS No 47/2003) requires municipalities to submit project plans and pre-feasibility plans which are eligible for state funding. Planning is a first responsibility of the municipalities. The Ministry provides 50 % of the funding for approved projects. Especially in the Southern part of the country water resources are limited, while restricted water tariffs prevent development and investment in water infrastructure projects. Water

⁶ National Environmental Strategy of the Republic of Serbia, draft, 17 June 2005, Directorate for Environmental protection – Ministry of Science and Environment.

⁷ Interview Directorate of Water 28 June 2006 with Mr. Vladimir Tanackovic – Head of Department for Water use and water Protection





tariff increases are less popular and water tariffs in Serbian municipalities are ranging between 10 and 26 dinars per m³. The average tariff of 15 dinars includes waste water treatment.

Up till now in only one municipality an attempt was undertaken to use a block tariff for the first 30 m³ with much higher tariffs for usage of water over this quantity. The use of water came down from 150 m³ per capita to 100 m³ per capita, which shows that water tariffs can be used as an instrument for water efficiency. However in other municipalities this situation does not exist.

Water is seen as a basic social service, while consumption is relatively high and tariffs are relatively low. The main problems are unaccounted water, estimated to be approximately 40 % also caused by leakages, lack of metering and illegal connections. The Directorate of Water is mainly functioning from a “fire fighter” position dealing with the most urgent areas without or with less water resources⁸. The Government participates in funding water and waste water sector projects by 50% while Municipalities provide for the other 50%. In special cases the participation of the Republican government is increased by 10%.

Total funding envisaged in the 2006 programme of the National Government:

1. Water supply systems: 580.000.000 CSD
2. Construction and rehabilitation of water treatment plants 260.000.000 CSD

Currently a new **Water Law** is under development and approval through which current problems are likely to be dealt with in the near future. The new Water Law expects PUC's to operate more as a market oriented organisation dealing with revenues and costs and efficient operations.

The linkages between local water management and local politics need to be less strong and one of the ideas is to require a professional level (civil engineer) for management of local water utilities.

An overview of the sector of water supply and waste water is provided in a Sector Review paper⁹ produced within the framework of the MIA program for the European Agency for Reconstruction (EAR) in Belgrade.

The National Environmental Action Plan

Currently work is done to elaborate and implement activities derived from the Strategy documents as mentioned above in the **National Environment Action Plan**¹⁰.

Related to the subject of the report two action plans are relevant:

- **Action Plan for protection of water**

For the transformation of the PUC's in this area will be relevant:

- Review of water law and related regulations
- Issuing of operational permits for all individual WWTP plants
- Adjustment of water charges to reflect full cost recovery
- Improve information for management and citizens

⁸ Program of construction, rehabilitation and maintenance of water management facilities in 2006 -Ministry of Agriculture, Forestry and Water-Directorate for Water

⁹ Sector Review paper on the Water Supply and Waste Water sector, Royal Haskoning - May 2006

¹⁰ National Environment Action Plan – EAR and Ministry of Science and Environmental Protection, 27 November 2006.

(Unofficial draft)





- **Action Plan for waste management**

For the transformation of the PUC's in this area will be relevant:

- Review of relevant laws such as waste law and law on packaging waste and related regulations
- Formation of 10 solid waste management regions
- Establishing inter-municipal cooperation and Inter-municipal Waste Management Council (IWMC)
- Development of guidelines for collection of data and waste generation management
- Preparation and adoption of regional Waste Management Plans
- Pilot studies for Municipal Waste Collection Plans
- Feasibility studies on separation of collection and treatment of municipal hazardous waste
- Studies and site selection for regional landfills
- Construction of regional sanitary landfills and transfer stations

All these activities will require strengthening of PUC's active in these areas and give indication of increased regional approaches

2.1.3 The Legal and regulatory framework

The legislation covering the water sector is laid down in various Laws and Ordinances and in a continuous phase of change reflecting the transformation processes in the country. The main documents are the **Environmental Protection Law** and the **Water Law** giving guidance to policies, implementation and monitoring of the sector.

Important is also the **Law on Local Self-Government**. According to this law, municipalities are responsible for operations, maintenance and investment in water supply systems and water sanitation services. For this purpose public utility companies are established to operate the services.

2.1.3.1 The Water Law

The Water Law of the Republic of Serbia is the most important legal basis for the protection of water bodies, water use, and water management. It governs the conditions for design, construction, operation and financing of water management activities. The law applies to all surface water and groundwater, including drinking water and thermal/mineral waters (Art. 1). The Law on Water of the Republic of Serbia regulates the protection of waters, protection from the pestious effects of waters, utilisation of and management with the water as a wealth of general concern, conditions and ways of doing the water management and inspection over the implementation of regulations of this law. The regulations of this law addresses on all surface and ground waters, including drinking water, thermal and mineral waters, as well as the boundary and transboundary water courses, both those between the Republic of Serbia and Republic of Montenegro, and those between the Republic of Serbia and other countries in the vicinity, except it is not otherwise issued by other legal acts. The law regulates that waters can be used only in a way that does not threat their natural characteristics, does not endanger the life and health of people, does not peril the wild plant and animal species, natural wealth and immobile cultural wealth.

Every investor is required to observe and abide by water management requirements. It is even emphasised that wastewater is to be discharged upstream of one's own water supply sources (Art. 14). The obtaining of requirements is necessary for the construction, modification and enhancement of





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sewerage disposal facilities (collection, channelling, treatment, and discharge of wastewater). This also goes for discharge into a sewerage system, but not for unpolluted rainwater and domestic household wastewater (Art. 15).

The prerequisite for a water management permit (permit under the water law) is a “declaration of consent”, which is granted by the public authority that sets the requirements, i.e.:

- The Ministry responsible for water management or
- The Municipality for small structures and properties

Declaration of consent from the Ministry of Health and the Ministry of Environment are also necessary for sewerage disposal facilities. Construction of the facility must begin within two years after the receipt of the declaration of consent. The permit also confirms that water management requirements are complied with.

The funding of water-related activities is outlined in Paragraph IX of the Water Law. Fees are levied for:

- Water use
- Protection of water bodies
- Irrigation
- Pumping and drainage
- Material excavation from water bodies
- Use of water-related objects (navigation on water bodies, power supply, etc.)

2.1.3.2 Environmental Protection Law

This Serbian Law was adopted in December 2004. Its content was harmonized with the relevant EU legislation. It provides:

- Protection of soil, water, air, forest, biosphere and biodiversity, plants and animals
- Mandatory environmental monitoring: the programmes have to be adopted and performed every second year (including air monitoring).
- Responsibility of the Serbian Government to establish the criteria for environmental measurements and regular reporting of the results to the Serbian Parliament yearly.
- The important obligation of 1% taxes on all new investments in objects that could possibly be the sources of environmental pollution, and will be used for environmental protection and promotion.

2.1.4 Institutional framework

Sector Ministry

The Ministry of Agriculture, Forestry and Water Management is responsible for the water sector as a whole. The Directorate for Water acts as the ministry’s representative. The Ministry of Health and the Ministry of Science and Environment Protection give their approval on planned projects.

The Directorate for Water under the Ministry of Agriculture and Water Management has overall responsibility for water management issues at the national level. The EAR particularly supports





strengthening the capacity of the Directorate of Water to implement corresponding EU Framework Directives. The responsibility for environmental issues lies within the Directorate for Environmental Protection under the Ministry of Science and Environmental Protection. Several other Ministries are responsible for regulations and policy development in infrastructure, such as legal aspects of construction, environmental issues, quality standards and other standards.

Regulator

No regulatory authority has been established for the water supply and sewerage sector. The Ministry has a special **Department for Water Inspection**, which tries to stimulate municipalities and PUC's in the water sector to deal with unaccounted water and installation of water meters. The main instrument for regulation is water tariffs which are monitored by the state and fall under a general price cap for communal utility services tariff increases, with annual guidelines by the ministries involved.

Municipalities/Operators

Municipalities are responsible for provision, operation, maintenance and investment for water supply and sanitation services. Municipal water supply and wastewater systems are operated and maintained by local Public Utility Companies (PUC-s). PUC's are basically state-owned companies, founded and managed by the Municipalities. The Public Utility Companies are responsible to the Municipalities for their performance. The Municipalities themselves operate under overall responsibility of the Ministry of Public Administration and Self-Government.

2.1.5 Main issues to be resolved

- New Water Law defining new roles and responsibilities for the water sector.
- Separation of policy maker and regulator
- Establish a Regulatory Body for the water sector.
- Institutional framework to develop public utilities in the water sector at local levels into efficient operations
 - Conceptual model for water sector utilities
 - Indicate key ratios for staffing and organisation
- Initiate sector wide benchmarking for water supply and distributions and sewerage of public utilities at local levels
 - Set up pilot projects with relevant stakeholders.
 - Establish database/ knowledge centre with clear rules on transparency and access procedures
 - Technical assistance to support benchmarking at local levels
 - Set up project for development of benchmarks
 - Disseminate results through information and training activities.
- Integrate benchmarking in more specific budget guidelines for water utilities also including tariff and wage developments related to efficiency ratio's





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2.2 District Heating Sector

2.2.1 Policy framework

The main policy in the field of district heating is an integral part of the Sector Policy for the Energy Sector Development Strategy of the Republic of Serbia by 2015.¹¹ This document has been developed as a background policy document for approval of the Energy Law in Parliament. The Policy gives an overview of the development of the energy system of Serbia at the end of 2002, assesses the energy needs and developments in the current situation and on the longer term, provides projections for the energy development needs by 2015 and determines the main priorities to secure energy for the Republic and its stakeholders. District heating is only a minor subject in the Report mainly focusing on providing and/or using new energy resources contributing to energy efficiency in the country

The report indicates as one of the main problems:

“the uncoordinated consumption and production of appropriate energy products, particularly during the winter period when, due to the heating of residential, working and office space, the needs frequently exceed the production capabilities of power resources and district heating companies.”

District heating systems exist in 45 cities of Serbia, consisting of decentralized heat resources with an installed power of about 6.000 MJ/s and appropriate distribution networks. District Heating is used for heating of residential and office space of about 450.000 equivalent flats (covering 66m² on average). One of the main problems in the sector is obsolete technology leading to low energy efficiency. According to this problem analysis for district heating systems the main priority is: rehabilitation of boiler room installations, heating pipes, distribution networks and house substations indicated with a necessary investment of USD 220. Within the framework of this technological upgrading (Priority 1) and increased energy efficiency and environmental protection (priority 2) are the main objectives of the program, which is also reason to develop new thermal resources and improve the use of current resources in the district heating companies.

Within the first priority, a need for an investment of € 180 million is envisaged for rehabilitation of existing boilers, district heating networks and individual heating substations. Within the second priority, approximately € 230 million is the estimated value of investment for connecting an additional 180,000 consumers to the district heating system.

2.2.2 Legal and regulatory framework

The legal and regulatory framework for the sector is laid down in the Energy Law¹² of 2004. The local self-government units have clear responsibilities in the Energy Law and must based on Art.7 produce Energy Development Plans determining energy needs and the terms and conditions for providing the necessary energy capacities in line with the Energy Strategy and programme.

¹¹ Energy Sector Development Strategy of the Republic of Serbia by 2015, Ministry of Mining and Energy, Belgrade, May 2005.

¹² Energy Law, Official Gazette RS No 44/2004





Chapter 12 in the Law is specifically dealing with Heat Production and rights and obligations of heat producers, such as District Heating companies.

- Article 142 indicates that heat distribution should be performed according to the principle of transparency and non-discrimination to all consumers within the territory.
- Article 143 holds the heat distributor responsible for maintenance, functioning and development of the heat distribution system, which have to be laid down in a 5 year development plan indicating the development and rehabilitation of the system.
- Article 144 requires heat distributors to adopt distribution system operations rules
- Article 145 requires heat producers to determine terms and conditions for heat supply continuity and rights and obligations for consumers.

2.2.3. Institutional framework

Sector Ministry

The Ministry of Mining and Energy is responsible for sector policy development in the Republic of Serbia. Due to the importance of the sector, the Government established the Agency for Energy Efficiency in 2004 to disburse small value grant funds (e.g. from the EAR) for service efficiency improvement. The Energy Industry in Serbia consist of oil and natural gas industry, coal mines, electricity power systems and district heating systems and industrial energy. The name of the Ministry indicates the importance of the coal sector for the country with main coal extraction and coal processing in three open pit mines of which 95% is used for power production.

Municipalities and PUC's

The Energy Law defines the principles for (re)organization of public energy enterprises into independent entities authorized for the performance of appropriate energy activities. Regardless of the fact that the operations of the district heating system greatly affects the needs of customers to use other more convenient/cheaper energy products, and thus the conditions of performance of other energy activities, heat generation, distribution and delivery is defined as a municipal energy activity remaining within the competence of local self-government.

Energy Efficiency Agency (SEEA)

The Agency proceeds with the programmes, projects and activities of the former Energy Efficiency Agency established by the Decree of the Government of the Republic of Serbia on 30 May 2002 and abolished on 15 May 2004. The Energy Efficiency Agency of the Republic of Serbia (SEEA) was formed by the new Energy Law put in force on 1 August 2004. The Energy Law defines the establishment (Article 146), duties (Article 147) and starting date of the regular operation of the Agency (Article 167).

The Energy Efficiency Agency is formed as special republic organization meaning separate legal entity. The Agency was registered in the Trade Court in Belgrade on 4 October 2004 and started regular operation by the same day.

The managing of the agency is carried out by the director who is appointed by the Government of the Republic of Serbia. The internal organization and job descriptions in the Agency are approved by the





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Government of the Republic of Serbia. The Agency submits an annual programme and reports on the operations to the Government of the Republic of Serbia.

The operation of the Agency is financed through the budget of the Republic of Serbia. The Agency is direct user of the republic's budget. The Agency uses also EU donations (provided through European Agency for Reconstruction, EAR) for financing part of its programmes and projects.

The overall objective of the indicated strategy programme is to provide the Government of Serbia with a number of targeted tools and measures for governing the development of the energy sector in Serbia in an energy efficient way.

The Energy Efficiency Agency carries out activities related to:

- drafting of proposals for incentive measures aimed at enhancing energy efficiency in the drafting of the Energy Development Strategy;
- drafting and proposing programmes and measures for stimulating rationale and efficient energy use; and monitoring their implementation;
- drafting proposals for implementing energy efficiency, renewable energy sources exploitation and environmental protection;
- drafting and proposing technical and other regulations for increasing energy efficiency;
- drafting criteria for equipment efficiency evaluation in use of energy and method of marking them in line with adequate international regulations and standards;
- providing financial and technical support in the preparation and implementation of priority energy efficiency projects;
- consultative, advisory and educational activities in promoting energy efficiency;
- other activities in compliance with the law.

Once a year the Energy Efficiency Agency shall report to the Government of the Republic of Serbia on its activities in the previous year and propose measures.

2.2.4. Main issues to be resolved

- Set up pilot projects on renovated boiler facilities for district heating companies targeting buildings with current relatively large share of energy consumption.
- Disseminate project results to all district heating companies in the country.
- Establish information system for exchange of key operational data to all district heating utilities.
- Prioritize projects for the modernization of infrastructure with increased energy efficiency with pay back period of 3 – 5 years.





2.3 Solid Waste Sector

2.3.1. Policy framework

The Policy framework for solid waste is formulated in a recent policy document¹³ National Waste Management Strategy approved in July 2003. This National Strategy is a basic document providing conditions for the rational and sustainable waste management in the Republic of Serbia. The Policy framework provides general and sector specific goals and objectives and determines principles of waste management implementation and planning.

Waste is generally classified as controlled and uncontrolled waste. Controlled waste includes domestic, commercial, and industrial waste, including medical waste. All the mentioned waste may be inert, hazardous or not. Domestic (household) waste which is not hazardous, is also classified as communal waste, collected within a certain area, usually the municipality. Uncontrolled waste includes agricultural waste, and waste from mining and quarry industry.

Important in the National Waste Management Strategy is the waste management policy analysis, which draws attention to:

- Waste volume development in the Republic of Serbia;
- Waste collection and main problems in this area;
- Waste treatment and lacking capacities in this field;
- Use of disposal sites as done currently and will be done in the near future.

One of the key instruments in the Waste Management Policy is the classification of deposit- sites as indicated below:

Class	Characteristics
K1	Big sanitary deposit-sites with complete equipment (draining systems and bottom sealing, systems for filtrate and gas monitoring and control on the site)
K2	Official disposal sites which may be used during long periods, provided they are reclaimed and reorganized in compliance with EU standards
K3	Official disposal sites – dumps which may still be used up to 5 years, provided renovation is done with minimal prevention measures
K4	Public disposal sites – landfills not fulfilling minimal protection measures, completely full, which should be immediately restored, closed and re-cultivated.

Based on this classification, efforts are undertaken to terminate K4 disposal sites, temporarily allow K3 sites and move into full development of K2 and K1 disposal sites. This implies also scale enlargement in waste management as there are currently over 180 disposal sites and many more illegal waste dumps, which will be terminated while increasingly using a smaller number of professional disposal sites for at least a number of 200.000 inhabitants thus forcing municipalities to work together on waste management modernization strategies and implementation.

¹³ The National Waste Management Strategy including the program of harmonization with the EU, Ministry for Protection of Natural Resources and Environment, Belgrade 2003.





One of the main PUC transformation issues in the implementation of the proposed program is the construction of regional waste management facilities in different areas of waste management. This implies that problems cannot longer be dealt with by one municipality, but have to be taken to a inter municipal or regional level with interest of all stakeholders and contributing to transparency and professionalisation of management and operations in these joint local public enterprises.

In the policy document other regional facilities are elaborated into regional clusters, based on mainly technical and economic criteria:

- The required network of regional landfills e.g. a total of 29 regional clusters for 160 municipalities;
- The network of transfer stations e.g. a total of 44 regional clusters for 63 municipalities;
- The network of recycling centres e.g. a total of 17 regional clusters for 160 municipalities;
- The network of fertilizing centres e.g. a total of 7 regional clusters for 146 municipalities;
- The network of incinerators for communal waste, e.g. a total of 4 incinerators for 160 municipalities

The indicated clusters are a recommendation to the municipalities, which may decide otherwise to form clusters with other municipalities.

Implementation of the Waste Management Policy

The implementation of the Waste management Strategy is detailed into different timetables for:

1.	Legislative instruments	Period 2003 - 2005
2.	Institutional and organization instruments	Period 2003 - 2015
3.	Technical/Operational instruments	Period 2004 - 2015
4.	Economic instruments	Period 2003 - 2005
5.	Development of public awareness	Period 2003 continued

2.3.2. Legal and regulatory framework

The National Waste Management Strategy document elaborates the future legal framework for the waste management sector. Regulations regarding waste management are laid down in numerous official documents and the Policy strives for an integral approach. The Policy document mentions a list of 40 laws, by laws, regulations which deal with some aspect of waste management in the Republic of Serbia. Until these laws are updated and brought to a more integrated level all of them are relevant to improve waste management. This relevance is detailed in the report.

The national Solid Waste Management Strategy 2003, including the program of harmonization with the EU, presents a legislative and institutional framework and economic instruments and a hierarchy of management of all categories of waste. The adoption of the National Strategy is to be followed by several implementation plans for the collection, transport, treatment and disposal of solid waste in a controlled and responsible manner. It also stresses the need for institutional and legislative capacity building, as well as education and increasing public awareness.

The National Strategy promotes the creation of regional landfills with the aim of decreasing the number of locations for waste disposal. The priority in program development will be given to Municipalities which





1) come to an agreement about cooperation on landfill construction, 2) have a suitable available location that meets environmental standards and 3) have projects for which the design has been completed.

A new Law on Environmental Protection is planned for approval in Parliament in October 2006. Also the EU legislation concerning waste management is listed and already fully taken into consideration.

2.3.2. Institutional framework

The institutional framework determines who the main players are and what responsibilities they have in the waste management sector. In the Policy document the following stakeholders are mentioned:

- The Ministry;
- Autonomous region's authorized agencies
- Regional self-governing authorized agencies
- Recycling Agency
- Authorized laboratory for waste research.

Ministry

In recent years the responsibilities for waste management have been attached to different set up of ministries in subsequent formation of governments. In the current situation the Ministry responsible is the Ministry for Science and Environmental Protection. This Ministry has two units involved:

- Directorate for Environmental Protection
- Agency for Environmental Protection

Policy-maker

This Ministry has the policy-maker role as indicated in its responsibility "to develop and suggest the waste management strategy to the Serbian government" and has also a role in approval of local government policies as it "adopts waste management plans on the level of several municipalities". For sector development it "coordinates waste management activities significant to the Republic and follows their progress"

Regulator

The Ministry has a supplementary role in sector regulations as it:

- Prepares regulations and technical standards;
- Issues licenses required by law and keeps adequate registers
- Coordinates activities regarding compliance with international agreements, regulations and decrees;
- Issues permits for waste import, export and transit.

In relation to both roles it is useful that the Ministry organizes the information system on waste on the territory of the Republic as the autonomous province does on its territory.





Operator:

The operator role is mainly allocated to the Self Government unit/municipality which:

- Develops the local waste management plan;
- Organizes, provides, manages and carries out waste management activities and services
- Manages the collection of service payments;
- Contributes to issuing of licenses and permits and takes part in decision making in regard to treatment plant building

Owner:

The founder of the PUC in the municipality is also the owner, but the main assets of the PUC's are owned by the Republic of Serbia. A decentralization process including transfer of assets will need a change in the Constitution. Most consultancy reports on developments in the sector agree on transfer of assets to the municipalities on the longer term as it will create conditions for the municipalities to have funding opportunities in using these assets in different ways. Closely connected to the ownership of assets is the valuation of assets to determine current values.

Recycling Agency for waste management

This Agency is set up as a supporting institute to check on:

- Monitoring and control of secondary raw materials;
- Market research secondary raw materials market
- Providing studies and analysis and set up data bases on secondary raw materials;
- Support in waste classification, gives support in waste classification into secondary raw materials and communal waste.
- Introduction of new technologies into the recycling process
- Educating the population on waste recycling options and methods.

Based on this the Agency is a kind of Technical and Professional Institute advising the sector stakeholders.

The Agency for Environmental Protection

The draft Law on Environmental Protection anticipates the establishment of the Environmental Protection Agency, which will perform the following activities:

- Analysis of waste management plans required for obtaining ecological permits;
- Analysis, development and maintaining a database on waste in the Republic of Serbia;
- Classification of waste into adequate categories according to the waste lists;
- Performing other activities as indicated in the regulations in the new Law.

Based on these functions the Agency is a kind of de-concentrated activity for the Ministry, which performs some monitoring and support functions in the process of implementation of the new Law.

The Policy report indicates institutional demands and sectoral integration as new challenges in the framework of implementation of the National Waste Management Strategy;





“Decentralization, together with advanced capacities of waste management, usually calls for innovations in organizational structures, human resources, planning and definition of local authority’s tasks. Identification of institutional restrictions is necessary in a system with increased competences and autonomy on a local level. Regarding urban areas, institutional organization depends on size and development level. Cities and medium sized towns have governance responsible for communal waste management. Municipalities have to join, in order to plan mutual waste management and more efficient waste disposal”.

The development of the legal and regulatory framework is seen as the basic factor to proceed with private sector participation, which is one of the priorities for this year.

2.3.4. Main issues to be resolved

- Set up pilot projects aiming at regionalization of solid waste treatment
- Capacity enhancement municipalities and PUC’s
- Stimulate PPP projects in the solid waste sector
- Disseminate project results to all municipalities and PUC’s in the sector.

3 PERFORMANCE OF PUC’S IN RELEVANT AREAS

3.1 Water sector performance

The Sector review paper gives an overview of sector performance and main problems in the water supply and waste water sector as indicated hereafter:

<p>Policy and sector development</p> <ul style="list-style-type: none"> • Overlapping competences state institutions • State owned assets of operators • Restricted tariffs decided at central level in political arena • PUC’s dependent on government for conditions for operations and maintenance 	<p>Standards /Technical Quality</p> <ul style="list-style-type: none"> • Incompatibility with EU Framework Directives or standards • Insufficient/inadequate treatment of water for drinking purposes • Very low level of monitoring operational performance • Lack of information systems for monitoring surface water and groundwater • High rates of unaccounted water
<p>Finance</p> <ul style="list-style-type: none"> • Low tariffs not covering costs of operations and maintenance • Cost of capital not taken into account • Underinvestment in system development 	<p>Environment/ other factors</p> <ul style="list-style-type: none"> • Inadequate protection of water intakes/reservoirs • Uncontrolled use of fertilizers causing pollution • Over-exploitation of ground water resources





It is clear that improvement of performance will mainly be a task for the PUC's and the municipalities involved. Some of the municipalities are active in improvement projects in the field of water supply and waste water.

For this reason we will now give attention to benchmarking efforts which will support the water sector operators to improve effectiveness of their organization and efficiency of their operations.

3.2 Benchmarking in the water sector

The set up of the monitoring of performance and benchmarking program of the Serbia and Montenegro Waterworks Association (SMWA) is based on the World Bank initiative for IB-Net, an International Benchmarking web site¹⁴ for water utilities.

For the collection of data at the start 20 key criteria are chosen:

Business process category	Performance Indicator	
A. Service coverage	1	Water coverage
	2	Sewerage coverage
B. Water consumption and production	3	Water Production
	4	Total Water Consumption
C. Non Revenue Water	5	Non Revenue Water
D. Meters	6	Metering Level
	7	Percentage sold that is metered
E. Network Performance	8	Pipe breaks
	9	Sewer System Blockages
	10	Losses
F. Operating costs & staff	11	Unit Operational Cost W&WW
	12	Staff W&WW/'000 W&WW connection
G. Quality of Service	13	Continuity of Service
	14	Quality of water supplied
	15	Complaints about W&WW services
H. Billings & Collections	16	Average Revenue W&WW
	17	Collection ratio
I. Financial Performance	18	Operating cost coverage
J. Assets	19	Gross Fixed Assets – water & waste water
K. Affordability	20	Purchasing Power Parity

As said the SMWA project is in an initial phase and still lacks clear institutional support and funding.

3.3 Energy sector performance

Current energy challenges in Serbia¹⁵:

- High energy consumption in buildings with large share of use of electricity for heating purposes

¹⁴ Web site <http://www.ib-net.org/>

¹⁵ Website SEEA <http://www.seea.sr.gov.yu/>





- Low energy efficiency in industry with out-dated energy-intensive manufacturing technologies
- Technically deteriorated, energy inefficient and polluting municipal energy supply services
- Low exploitation of the available potential of renewable energy sources
- Unsustainable financial operation of energy supply companies due to energy prices not reflecting actual production costs
- Need for large investments in the energy sector to improve and modernize energy infrastructure
- Need to develop and implement a comprehensive policy designed to improve energy efficiency and the utilisation of renewable energy sources

District heating companies providing services in municipalities

The Serbian Energy Efficiency Agency has developed the Strategy Programme 'Energy Efficiency in the Municipal Sector' which should contribute to the increase of energy efficiency in the buildings and systems which are within the responsibility of the local (municipal) administration. No specific data are available for each of the district heating companies. The main links between the current district heating companies come from using common resources for generating energy and benchmarking results with renovated facilities and key parameters for district heating operations.

3.4 Solid waste sector performance

The sector performance analysis in the Waste management Strategy report reveals many of the problems with waste management in the country ranging from lack of access in terms of coverage, lack of facilities, monitoring systems, professional approach to recycling and waste management treatment etc. For each of the activities a full list is elaborated and it is fair to say that basic awareness of what should be done is relatively well developed.

The problem analysis is serious enough to have an overhaul of waste management systems on a higher scale than that of single municipalities to realize essential economics of scale for a viable service activity to the community and professionalization of management of services at the same time.

The implementation process has just started as old sites can only be closed after new ones are set up. Implementation encounters various difficulties but with a balanced "sticks and carrots" approach the responsible municipalities are tempted to develop regional approaches.

In the framework of improvement of waste management activities private sector participation is envisaged taking different forms such as private sector participation through outsourcing services, hiring external management and temporary licenses based on performance and service level agreements. Another possibility is using BOT contracts or variations like ownership, reconstruction, renting, design and financing, etc.

The role of private sector enterprises is especially seen in:

- Use of advanced technical and management expertise;
- Introduction of new technologies
- Increased efficiency
- Construction of bigger capacities and facilities
- Reduction of cost of public subsidies
- Advancement of service quality





In the framework of the GTZ project for "Modernisation of Municipal Services" a first Public Private partnership (PPP) project has been realised in the field of solid waste collection and disposal.¹⁶ Partners are GTZ as co-funding institution, Trojon & Fischer EKO as a private sector company and 4 municipalities in East Serbia. Trojon & Fischer EKO is a private mixed Serbian/German company, providing services of solid waste collection and disposal from 2004 in accordance with the current standards of environmental protection. The project is established based on a **concession** for handling the municipal solid waste for a period of 25 years. All participating municipalities did not have a structured waste management approach before and were faced with new activities on their territory. As the project has recently started it is still too early to assess the results on this PPP project in waste management.

4 CONCLUSIONS ON SECTOR POLICIES

4.1 Introduction

In our view institutional strengthening has to support improvement of institutional efficiency and effectiveness, which can be done at two levels:

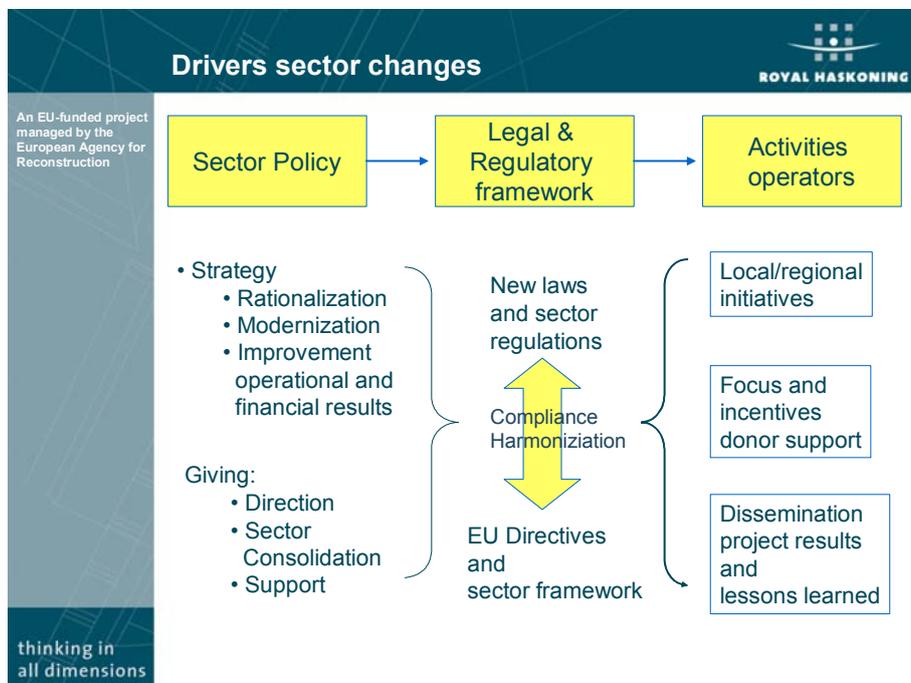
1. Creation of transparent and efficient organisational structures of the public utility companies
2. Proper allocation of tasks and responsibilities among key players such as the central government, the regulator, municipalities and other stakeholders.

4.2 Proper allocation of tasks and responsibilities

PUC's can be seen as operators in public services and the functions and responsibilities of authorities involved can be analysed based on the framework of separating roles of policy makers, regulatory authorities and operators hereafter.

¹⁶ GTZ brochure on PPP project in field of solid waste management with Trojon & Fischer EKO, 2006





Sector Policy functions as the main driver for sector development providing rationale for sector development, and giving direction for sector upgrading and modernization programmes, supported by law enforcement and other regulatory efforts to ensure proper implementation. Policy and regulatory efforts are leading to increased activities of sector operators and supported by activities for donor support.

4.3 Policy makers in relevant sectors

As for the main policy makers we have assessed the different policy makers and policy documents providing relevant sector policies.

- Ministry of Agriculture, Forestry and Water Management
 - Master Water Plan
 - New Water Law and policy paper under approval
- Ministry of Science and Environment
 - National Environment Strategy
- Ministry of Mining and Energy
 - Energy sector development in Rep. of Serbia by 2015
- Ministry for Science and Environmental Protection
 - National Waste Management Strategy



Based on the assessment phase we have drawn the following **conclusions**:

- From problem analysis it is clear that many challenges of institutional strengthening of PUC's need to be addressed at level above single local self-government units (municipalities)
- Sector policies show clear tendency towards up scaling and regionalization for local self government units and PUC's to be efficient and effective.
- Sector Policy water sector still to be approved with new Law on Water, which is assumed to address regional approaches to water supply and sewerage.
- In Republic of Serbia it is not likely to have one administrative intermediate level (autonomous province/ county/ district) for all sectoral approaches between central government and local self- government
- Trend is towards guided and voluntary association of local self-government units based on differences in rationale per sector

5 CONCLUSIONS ON REGULATORY FRAMEWORK

5.1 Regulatory Institutions

As for the identification of sector regulators we have assessed the roles of different institutions providing regulatory support to sector policies in the country:

- Water Supply and Sewerage
 - Ministry of Agriculture, Forestry and Water Management
 - Policy and Inspection
 - Ministry of Science and Environment
 - Environmental Strategy
 - Monitoring the environment provides horizontal coordination mechanisms

The main focus is on:

- Water supply and distributions with increased coverage for population;
- Water quality improvement;
- Waste water standards are issues at national level.

Main issues of attention are:

- Investment
- Service levels
- Tariffs
- Complaints handling have to be decided at local levels

Current activities under preparation are finalization and adoption of the Water Law and the Law on Financing of Water Management, preparing regulations derived from these laws, granting operational permits for individual WWTP plants and adjustment of water charges to reflect full cost recovery. Other important topics are application of drinking water standards with the EC Drinking water Directive 98/83/EC, self monitoring of suppliers, improvement of enforcement by authorized institutions, such as in Serbia the Health Protection Institutes. Future law enforcement will need strengthening of regulatory institutions, such as Department for Water Inspection.





- District Heating
 - Ministry of Mining and Energy
 - Policy development to use optimum of resources
 - Energy Efficiency Agency (SEEA)
 - Monitors compliance with the Law and regulations

Main issues of attention are:

- Investment
- Choice of main resources
- Service levels
- Tariffs have to be decided at central levels

- Solid Waste
 - Ministry for Science and Environmental Protection
 - National Waste Management Strategy
 - Recycling Agency
 - Monitoring and control of secondary raw materials

Current activities are prepared for the Waste Law and Packaging and Packaging Waste Law, preparing regulations derived from these laws and training of government institutions and other stakeholders in monitoring and law enforcement. Future law enforcement will need strengthening of regulatory institutions, such as the Agency Environmental Protection.

Based on the assessment phase we have drawn the following **conclusions**:

- New sector policies lead to increased need for implementation of law enforcement and monitoring of sector regulations.
- Law enforcement will take some more time as institutions need time to catch up and have to create conditions to follow up on policies.
- Most projects are aiming at construction of facilities, for which each sector shows high needs, while functioning of municipal entities involved and operational and financial results are issues for the longer term.
- Examples of sticks and carrots approach in solid waste sector seems likely for other sectors as well:
 - Carrots : priority in investment and funding support
 - Sticks :law enforcement with fines and penalties
 - Balanced combination of instruments above
- Clear need in support to strengthening of regulatory institutions, but regulation will only have effect after phase of reconstruction and upgrading of technical infrastructure and certain conditions are put into place for proper functioning of public utilities.

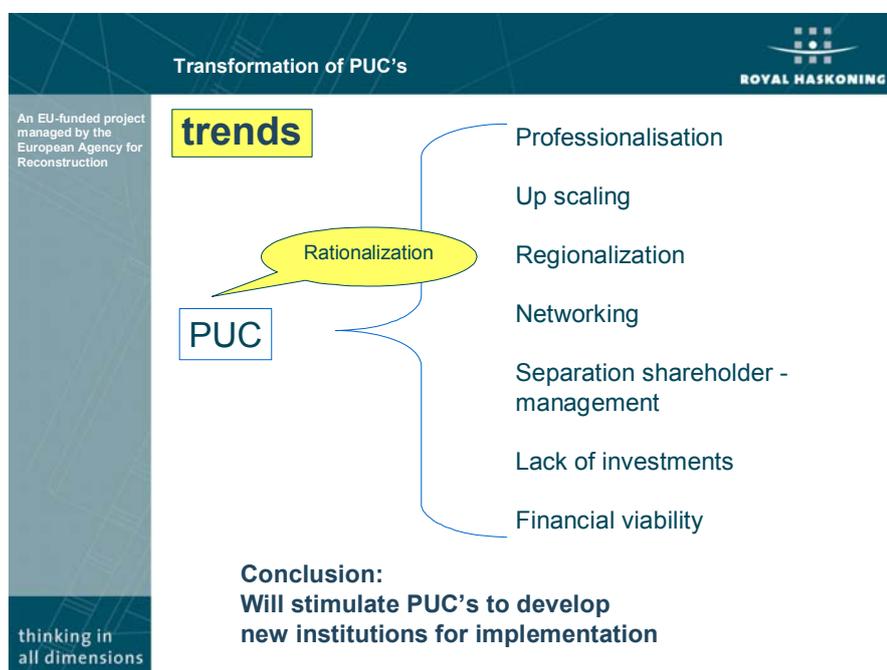


6 PROPOSED STRATEGIES FOR IMPROVED PUC PERFORMANCE

6.1 Operators in public services

As described in the Law on Self Government of 2002 Municipalities are the founders of public enterprises (PUC's), while the legal obligations of the PUC's are laid down in different laws regarding public entities.

The sector policy framework and legal and regulatory framework must provide guidelines for the improvement of operational and financial performance of public utilities. Currently new sector policies indicate a drive towards rationalization of PUC's as elaborated in the next overview:



The **Rationale for up scaling and regionalization** is mainly based on:

- Water Supply & Distribution and Sewerage
 - Expected in new Water Law to be addressed in relations within river basins as derived from EU Water Directives and/or economics of scale for viable projects in this sector
- District Heating
 - Related to larger local self government units without grouping of municipalities or related only to connected municipalities.
- Solid Waste



- Sector Policy provides clear framework for regionalized approaches which rationale is different per activities (landfills, transfer stations, etc.) involved, but leaves room for local self-government units to find cooperation

6.2 Problem analysis PUC's

From the different reports on projects concerning the local public services a range of underlying issues can be derived needing attention in institutional strengthening of public utilities.

Subject area	Topics
Ownership	<ul style="list-style-type: none"> • PUC main bodies such as Supervisory Board and Management Board are in principle political bodies with representatives appointed by the municipality. • PUC assets are valued according to general rules on public enterprises including indication of historic value including annual depreciation on the Balance Sheet. No other depreciation methods are used. • PUC's have no ownership on assets used by the utility companies, but have "usage rights", which implies that they cannot use commercial value of assets in attracting loans and private sector investments. However they are allowed to agree on contracting loans and issuing loan securities and guarantees.
Management	<ul style="list-style-type: none"> • PUC policies may be seriously affected by partisan politics and continuous political interference with municipal elections having great impact on review of utility policies and operations. • Top management is appointed by the owner the municipality and management changes frequently with change of executive management of the municipality (Mayor) or change in balance between political parties. PUC management is as such seen as a political related function and less as a professional one. This is the case as important decisions on PUC operations need approval of the Municipality, such as scope of services, investment, tariffs, and budgets. • Management of public utilities have to be based on Business Plans, while only few of public utility companies can provide such plan, or take efforts in the framework of donor funded projects as required in the conditions for the projects. Sector policies are increasingly pushing forwards with planning instruments at local levels. • Support systems of public utilities in all fields have to be improved to provide better information for management strategies and decisions. • Management of public utilities is in general not yet based on benchmarking of public services neither within the country, not with comparable companies abroad.
Services	<ul style="list-style-type: none"> • PUC's are generally focused on providing basic public services but are not yet able to cover all target groups with public services also due to geographic conditions in the country and lack of investments. • PUC's face difficulties to catch up with modern requirements (standards, quality levels) for public services as most PUC's are in high need for investments for upgrading of facilities. • PUC's are generally not seen as customer oriented and service oriented organisations and have to develop in that direction.
HRM policies	<ul style="list-style-type: none"> • Staff of the PUC is on the pay roll of the public utility, but on the budget of the municipality which may influence social aspects of providing and maintaining employment in the municipalities involved. This may limit the drive towards efficiency and effectiveness of the PUC's. • In current cooperation projects not much attention is given to increase productivity of all staff involved in merging processes and operations.





Finance	<ul style="list-style-type: none">• Pricing of public services is not based on real cost, but on political decisions of the municipality leading to subsidization of public services.• Pricing of public services is based on a general price gap related to inflation on annual basis provided by the Ministry of Finance. There is no sector approach to pricing.• Based on Law of Enterprises PUC's are obliged to produce Annual Accounts and transfer them to the Central Bank, such as:<ul style="list-style-type: none">○ Balance Sheet○ Profit & Loss Account○ Cash flow Statement <p>The information provided to the central database are not made accessible for outsiders and do not create transparency in countrywide financial results of public utility companies.</p> <ul style="list-style-type: none">• PUC's have as a main objective to fulfil the budget agreed upon with their owners the municipalities. PUC's operate without profit motives, which may limit drive towards improvement of efficiency and effectiveness.• Many PUC's show deficits on their budget and to not contribute to municipality budgets. Municipality budgets are tight and do not provide investments in local infrastructure development and modernization.• Unaccounted fees for services provided are a political issue in all municipalities. Law enforcement is a political and sensitive issue, however now increasingly addressed.• PUC's have in the past not been able to reach full cost coverage of services and have to find ways to catch up with cost coverage requirements. Even cost coverage is not enough as PUC's also must realize funds for new investments and upgrading of technical infrastructure and facilities. PUC's have in principle to become financially viable enterprises.
Alliances	<ul style="list-style-type: none">• PUC's have based on current laws options for:<ul style="list-style-type: none">○ Establishing and invest in new public utility enterprises○ Enter into joint ventures, alliances and PPP's with approval of central government• Municipalities may differentiate between core and non-core activities and have options to outsource non-core activities based on contracts to public sector operators. This implies that for smaller activities such as public park maintenance, snow removal, street cleaning public operators can takeover public activities previously done by PUC's.• Considering the need for investments in the development of the infrastructure and quality of services in the relevant sectors investments and alliances with private sector operators may bring progress and sector consolidation.
Inter-communal cooperation	<ul style="list-style-type: none">• As for establishment of inter-municipality or regional public enterprises PUC's have to establish new legal entities within the scope of current laws. With a greater number of PUC's participating into the new legal entity political representation becomes more difficult.• Inter- municipality public utilities address mainly issues to be arranged in the set up phase of new constructions and facilities, but the question remains if they provide solutions for the longer term to become efficient and effective enterprises.

In the next paragraph more attention will be given to proposed developments in the transformation of public utilities to address common problems as experienced in the functioning of PUC's as mentioned above.





6.3 Creation of transparent and efficient organisational structures of the PUC's

Utility companies are in general seen as providing basic services and in the current phase of development main efforts are directed towards reconstruction and updating technical infrastructures seriously affected by enduring conflicts in the last decade. Beyond this the public utilities face serious reform in the way they used to operate and towards modernised operations in a development towards a market oriented economy.

The Main challenges for future PUC functioning are:

- Increase coverage of services for population at large.
- Ensuring further reduction of cost of services.
- Obtaining optimal scale in service delivery, and
- Exercising effective regulation and supervision over private providers of services

Based on the assessment phase some common problems or challenges can be identified:

- Need for better Corporate Governance
- Need for better Management procedures
- Need for Strategy and Business Planning
 - Need to improve operational performance
 - Need to improve financial performance
- Introduction of Customer Management
- Development of Human Resources
- Increasing need to respond to Inter-municipality/regional approaches to utility services

6.4 Assessment ownership and ownership rights

The new law on LSG has introduced a considerable degree of financial decentralisation, granting municipalities the right and responsibility to manage transferred and supplementary revenues, but has not solved the problem of ownership. Municipalities have the right to possess land, business facilities and assets owned by the Republic.

Currently, there is confusion over this question of ownership of assets, particularly business facilities and building areas that are handled by the municipality. The Constitution still asserts state ownership over assets, while granting municipalities' usage rights.

Based on the assessment phase we have drawn the following **conclusions**:

- Rights and responsibilities split between municipalities and the Republic
- It is recommendable to combine at single level of government
- Will minimize potential for confusion in relation to institutional capacities
- Management Board of utilities must be held accountable by municipality, but not be involved in day-to-day decisions
- Approval of and monitoring of performance to be based on (5 years) Business Plan

It is also expected that the new Constitution will address this issue for the near future.





6.5 From local government to local governance

To strengthen the position of public utilities it can be considered to embark on Corporatisation of PUC's, just has been done in the public sector in many countries in the EU in the last decades.

The point of departure for the strategy on PUC's is the analysis of the existing situation. There are many constraints for the reform process, regarding limitations in the current legal environment, financial situation of the utilities and their assets' status as central government assets, as well as 'social' problems: lack of knowledge and understanding, expectations of municipalities, and the experience so far with the consolidation process.

It will be necessary to work on the current problems in ongoing projects directed towards creating new public infrastructures and establish the conditions to go into this direction. A balance between problems and challenges may lead towards a new strategy of transformation of public utilities.

What can be the **driving factors** for the elaboration of the PUC Corporatisation strategy?

- Public administration reform policy, assuming transfer of more power and assets to municipalities,
- Institutional effectiveness of incorporation, as it puts utilities on the basis of an enterprise
- Financial viability and good governance of the companies,
- The need to obtain investments for the public sector, especially with options for increased private sector involvement in management of utilities,
- Work done in the sector so far (starting consolidation), and
- Efficiency of the incorporation process, which will create a framework as used by commercial enterprises working for customers in the marketplace.

The Transformation vision is built of several elements – strategic options. Recommendations with regard to the strategic options are the following:

- **Level of consolidation of the sector:** sector policies are aiming at public enterprises for larger areas to justify investments, get a reasonable ROI and have the economics of scale to provide professional services with new technologies.
- **Ownership of public companies:** In the long-term vision the municipalities and not the central government become real owners. The shares of individual municipalities have to be substantial in order to provide the perception of ownership and municipal investments. Increasingly private sector operators will be involved also providing necessary investments in the infrastructure of the sector and contributing to improvement of management and operations.
- **Legal forms of corporate entities:** a form of Limited Liability Company seems more appropriate for the water and solid waste sector, especially if assuming for the time being municipal ownership of the companies. As a Privatisation strategy is not yet accepted new legal forms for the entities to be created will have to comply with current laws on communal enterprises and on local self-government. On the longer run also more joint stock companies can be established enabling utilities to open up to private sector involvement with major stakes in capital and management.





- **Space for Public-Private Partnership / Private Sector Participation:** some forms of PPP / PSP should and will be present in the future. However, it is assumed that in the foreseeable future the available options will not go beyond Lease or O&M Contracts – and even this will require amendments to the existing legislation.
- **Institutional structure or roles to be played by key stakeholders of the sector:** clear allocation of roles – policy setting and supervision belonging to the government (with no ownership in the sector), ownership and investments are municipal (no direct involvement in operations), an independent regulator setting tariffs and issuing licenses on the basis of the government’s regulations. (As dealt with in previous chapters).

6.6 General framework for Corporatisation

To indicate the impact of Corporatisation the following framework is used. This framework puts the legal status of entities on a scale from full government/state governance towards full private sector/market governance based on some key issues, such as:

Ownership:

One of the main issues is the ownership of the legal entity whether fully an integral part of the public administration (such as a Ministry department and or Regulatory Body), or set up as a state utility fully owned by either by the central, regional and/or local government or at the other end of the scale companies having minority or majority ownership with private sector parties.

Rule of Law:

The governance of the legal entity may be based whether on Public Law or at the other end Private Law. An example of the last category is commercial law as a basic framework for functioning of enterprises operating in the marketplace.

Legal status:

Based on both key issues above legal entities may have a different legal status as part of the Public Administration, a Public Utility, a Public Enterprise, a private company and/or a global company operating in many countries.

ownership	Public Ownership		Private Ownership		
rule of law	Public Law		Private Law		
legal status	Administration	Utility	Enterprise	Company	Industry player Global brand

Corporatisation is a crucial transition from public law to private law putting legal entities in the position as a corporate entity operating in a marketplace and in competition with other providers. This market may show many differences in each sector on a scale of monopoly to oligopoly characteristics or impact of the profit motive on its operations.

A good example is telecommunication long seen as a public utility now operating is a fully privatised company, many of them having to compete in increasing global markets. The water sector is usually at the other end operating as public owned entities providing basic services. However while in some





countries water utilities have a legal status as public utility in many countries the legal status is changed as a result of a corporatisation process in a public enterprise.

A public enterprise may show a mixture of both key issues mentioned above as it is based on private law, but also still may have dominant public (government/state) ownership. As a result of Corporatisation also private sector involvement may increase from minority stake into majority stake, which marks the transition into privatisation.

The crucial issue is the internal drive of the different legal entities, which has influence on position of management, use of management tools, business planning and work planning, finance and accounting and many other issues of its operations.

In the following scheme an overview is provided how the legal status may have impact on its functioning and operations. The overview is a general one, which may be tailor made to the sector involved.

It is also useful to say that transition may be a gradual one based on how governance by main stakeholders is applied in real practice. However each legal status has a fundamental impact on management and performance.

status aspect	Public Administration	Public Utility	Corporatisation	Privatisation	Globalisation
ownership	government	full state ownership	> 50 % state owned	< 50 % state owned	multiple share holders in many countries
main focus	represent State	represent Company	represent Business	represent Industry	represent global player/brand
finance governance	State budget	Sector budget	Strategic Plan	Business Plan	ongoing Business Planning
main drive	Law driven	Technology driven	Service driven	Market driven	Global market driven
drive regulation	state bureaucracy	sector authority	separate sector roles	Industry regulations	WTO/GATT trade agreements
dominant culture	public service	marketing	PMC's	branch/account management	country and PMC management
organisation structure	organic growth	functional structure	result responsible	business units	combination country/BU
HRM policies	civil servants	public sector employees	private sector employees	company employees	industry employees

A crucial transition is the change from public utility into a public enterprise, which focuses on efficient and effective service delivery based on management tools as used in private sector companies.

As a result this type of entity is put at arm's length of political interference which in general contributes to its operational and financial performance.





6.7 Advantages Corporatisation of public utilities

As main advantages of Corporatisation of utilities can be indicated that it will transform public utilities into legal entities, which will operate as enterprises with more immanent drive towards increasing efficiency and effectiveness, more open to consolidation of the sector and better positioned to attract private sector management and capital. The main legal forms in the incorporation process will be either set up of a Joint Stock Company or set up of a Limited Liability Company, depending on assessment on how much opening to more private sector involvement will be needed in the near future.

In the next scheme a comparison is made of main aspects of the institutional framework of incorporation compared with the current legal status of public utilities in Serbia.

Corporation	PUC based on current laws
<ul style="list-style-type: none"> ■ Legal entity based on commercial law ■ Clear business structure ■ Undisputable legal title to assets <ul style="list-style-type: none"> ■ own balance sheet and P&L ■ related to value of assets ■ Concrete own capital (equity) related to the value of assets ■ Business form allowing better management: ■ External regulations defining responsibilities of public organs; ■ More autonomy for the company; ■ Less political interference ■ Operations will be done based on contract management, such as service level agreements (SLA), and will tend to reduce political aspects of service operations. ■ External auditing 	<ul style="list-style-type: none"> ■ Legal entity based on public law ■ No business structure ■ No legal title to assets pending transfer of central government <ul style="list-style-type: none"> ■ no valuation of assets ■ mainly historic value of assets ■ Public entity limiting better management ■ Many unclear regulations and limited law enforcement because of framework ■ One to one (political) relationship with municipality ■ Much political interference under influence founder ■ In case of regional projects involvement of many administrative bodies having influence on the new utility ■ External auditing just recently obliged.

6.8 Some comparisons in water sector with other countries

In September 2003 a Comparative Review¹⁷ of Water Sector Restructuring in the EU Accession States, was finalised which gives some insight in developments in other countries, concerning policies, liberalisation of the sector, commercialisation, private sector involvement and topics of specific interest in the water sector.

¹⁷ Comparative Review of Water Sector Restructuring in the EU Accession States, Work Package 1, Final Report EU FP5 "Intermediaries" Project September 2003.





Trajectories of Restructuring

- There has been a widespread emphasis on the decentralisation of the ownership, management and regulation of water and waste-water/sewage utilities, though there is also large variation in decentralised in principle and decentralisation in practice.
- Commercialisation has been pursued to improve water sector efficiency, sometimes through private sector involvement, as a condition to secure grants/loans and in exceptional cases, as an alternative to private sector involvement.
- There are four main groups of countries in relation to private sector involvement as: first, widespread; second, being actively developed; third, limited; and finally virtually not existent.

Challenges for Restructuring

- Seven key challenges facing the current restructuring of the water sector are identified: the implications of multinational involvement in local water supplies; the implications of involvement by lending bodies; the difficulties of increasing water tariffs to cover costs; the capacity of municipal level organisation; the variations between geographical areas of municipal capacity; the difficulties of developing and ensuring effective regulation in an increasingly fragmented context; and finally the role that donations might play.

The Future of Restructuring

Three particular challenges will be important to the future processes of restructuring:

- how an increasingly fragmented water sector can be coordinated to ensure alignment with relevant European policy objectives.
- how appropriate capacity and expertise within Accession States will be developed to ensure that local priorities and concerns are protected.
- how increased public debate will be achieved about whether private sector involvement will lead to more investment in aging infrastructure networks and what alternative methods for increasing investment there might be.

6.9 Increasing inter-municipal cooperation

As stated before sector policies indicate an approach to improvement of public services with the construction of infrastructure and facilities beyond the level of single (smaller) municipalities.

This implies that in ever more projects municipalities have to work together in funding, management and operations of public utilities in their region.

Just an example is taken from the approved National Waste Management Strategy, which indicate over 100 inter-municipality cooperation efforts covering different combinations of municipalities just in one sector.

Example Solid waste Management Strategy

- Regional landfills e.g. a total of 29 regional clusters for 160 municipalities;
- Transfer stations e.g. a total of 44 regional clusters for 63 municipalities;
- Recycling centres e.g. a total of 17 regional clusters for 160 municipalities;
- Fertilizing centres e.g. a total of 7 regional clusters for 146 municipalities;
- Incinerators for communal waste, e.g. a total of 4 incinerators for 160 municipalities





From assessment of different projects¹⁸ it becomes clear that inter-municipal cooperation in the current situation is a relatively new phenomenon and not an easy issue, as municipalities are used to have direct influence on the PUC's in their area and are not likely to give up political control over these institutions. Working in new projects with a larger scale or regional projects involving a great number of municipalities implies that all administrative bodies of current PUC's or current municipalities may in principle be involved in the new utility (See also paragraph hereafter) and all municipalities can block progress in finding solutions for problems with specific interest for each of them.

Conclusion:

With new sector policies in other sector as well also aiming at regional approaches it may be the right time to develop a Transformation Strategy for public utilities which goes in the directions of incorporation of public utilities, putting them on conditions for market-oriented enterprises with more drive towards increasing of efficiency and effectiveness and opening up for private sector involvement in investments, management and operations and at arm's length of political institutions.

6.10 Model Inter-municipality Cooperation Agreements

In practice the need for inter-municipal cooperation is covered with (draft) model cooperation agreements, which for the time being have to be based on current laws concerning responsibilities of local self-government units, such as municipalities and current rules regarding PUC management. Based on such models the Cooperation Agreement can be tailor made to the project concerned.

Draft Multi-Municipal Agreement on Regional Cooperation¹⁹

According to all data that was collected during the project development, it was obvious that for the regions in Eastern Serbia is necessary to determine authorities for waste collection and disposal. Taking this into the account and the available case studies, the Model for cooperation agreement (Annex 3b) was made.

This model consists of 6 sections, dealing with the specific issue, e.g. collection organisation, financing of the scheme, etc.

- Waste collection, disposal and management of disposal site: this section describes the options for delegation of the responsibility of landfill management. Option A) Regional Utility Company that would be founded by participant municipalities; or option B) Public Utility Company of the municipality where the landfill is. Both options are suggesting that work force utilization for the new activities should include it from the whole region. The waste collection should be organised on municipal level and public (utility) companies should continue doing it.
- Inter-municipal board: this section is describing the possible responsibilities and liabilities of inter-municipal board. The members coming from each municipality should form the board. The board should be supervising the performance of the regional waste management scheme and company in charge of landfill management. It is body that would handle all disputes and raised issues by the board members. The section is suggesting how to make a good social programme of taking over the employees from the regional waste utilization company once the agreement is outdated.
- Financing scheme: it is suggested that the municipality should co-finance the scheme by contribution pro rata population and local mean income of individuals.
- Withdrawal of the parties: this section defines the terms of parties' withdrawal and the terms of breaking the agreement.
- Closing remarks: this is the section that is defining general issues such as entering into force, the period of

¹⁸ Annex 5 Case studies of projects in relevant sectors.

¹⁹ Source: Technical Assistance to the Municipal Support Programme Eastern Serbia, MSP-ES – Waste management Final report, January 2006.





agreement validity and disputes resolution.

As previously mentioned, the model was developed by taking into consideration available agreements in Serbia and the model developed by Urus Fuhrmann and Dejan Davidović, as a part of Modernization municipal services project.

The strength of the model is introduction of the precise delegation of responsibilities for waste management authorities. The weakness of it is that it can not be applicable on the beginning of the negotiation as it implies a lot of details that need careful planning.

As the initial document a Letter of intention (Annex 3a) could be utilized as it only stipulates the further common development of plan for the region.

Conclusion:

Especially the last remarks made on the use of inter-municipal cooperation agreements is relevant as the need for inter-municipal cooperation occurs in the phase of set up of new regional projects for the sector.

In some cases only Intention Agreements could be agreed upon as the establishment of the new utility requires much more detailed information and will be the result of a much longer process of development between the municipalities concerned.

This implies that such projects are under pressure of obligations of sector policies imposed on development of activities, but also obtaining funding for investments either from the state budget or from donor organizations.

The main stakeholders, the municipalities are not likely to give up political control over the public utilities but have to find agreement to get started and get funded.

While main issues are arranged for the starting period, still many issues have to be addressed for the (longer term) management and operations of the public utility. The Inter-municipal Board replaces direct interference of bodies of all participating municipalities, which would make progress very difficult as each stakeholder may find an argument to discuss own interests at any time in the project.

However in the long run it would be better to put agreement on services from the public utility on business conditions and a contractual basis (e.g. based on service-level agreements) than to continue working with possible political interference of numerous bodies of all municipalities involved.

Regional projects do not seem to start from a 'Greenfield' approach (starting as a total new regional concept and new organization, while taking into consideration current limitations in the implementation phase) or with the objective of a full merger of all activities (putting all activities, management and staff together in a new concept) of the existing public utilities. This also confirms that political conditions play an important role in the establishment of such projects, not necessarily aiming at optimizing efficiency and effectiveness of the public services right from the start.

6.11 Assessment of Inter-municipal Cooperation Agreements

In this paragraph we will assess the draft model inter-municipality agreement to find many aspects still to be elaborated in the course of the project and upon establishment of the new public utility.





This (draft) model agreement was used in the Municipal Support Program Eastern Serbia to conclude on cooperation agreements between the participating municipalities. As such inter-municipality agreements begin to emerge the first draft model agreements bear all difficulties to find common ground on “terra incognita”.

In practice the draft model inter-municipality agreement can be used as a basis document starting negotiations between all stakeholders in the project, while tailor making them to the needs of the projects.

However the problem issues will need to be addressed in the transformation of public utility companies. In the further operations of PUC’s other and more problems will need to be resolved and lessons learned should be exchanged between stakeholders through their own platforms such as SCTM and other interested parties related to specific sectors.

Laws

The draft Cooperation agreement is based on current laws such as:

- Law on Self-Government Art 12 Par 1 and 2 (Official Gazette of RS numbers 9/02,33/04 and 135/04);
- Law on Communal Activities, Art. 7 (Official Gazette of RS, numbers 16/97 and 42/98)

This implies that the agreement fulfils the obligations as laid down in relevant current laws of the country.

Note:

It is interesting to note that the provided options to establish either a joint PUC or accept one of them as the lead PUC stays very much within current Law on Self-Government, while for new legal entities on a regional scale also new legal forms could be taken into consideration, such as for instance a Joint Stock Company with or without a dominant stake of the private sector. No examples are yet known where this has been applied.

The issue of involving a Strategic Partner from the Private Sector as such as not dealt with in this Agreement, while it also does not mentions assessment of current options such as outsourcing based on concessions and outsourcing management contracts.

From the side of KOMDEL was mentioned that current projects involving strategic partners on the basis of concession agreements were difficult as agreements could be evoked halfway as a result of change in the political landscape after elections and with municipalities blocking further support.

Main options for inter-municipal cooperation

Option A - Joint PUC	Option B - Leading PUC
Municipalities agree to make all necessary decisions and establish a joint public utility company that shall manage the landfill on locality of municipality xxx. The company will have its seat in municipality xxx.	Municipalities agree to make all necessary decisions that the public utility company located in the municipality xxx shall manage the landfill
Municipalities agree that after construction of the regional landfill and establishment of the company they will stop	Municipalities agree that after construction of the landfill and establishment of the company they will stop using





using the existing landfills located within their municipalities	the existing landfills located within their municipalities.
The use of the landfill shall continue if there are conditions for that in terms of a construction of a transfer station on that location or some other infrastructural element for waste management.	The use of the landfill shall continue if there are conditions for that in terms of a construction of a transfer station on that location or some other infrastructural element for waste management.
The Joint Stock Company shall perform assigned tasks on disposal of solid waste from the territories of the municipalities	The Public Utility Company xxxxxxx shall perform assigned tasks on disposal of solid waste from the territories of the municipalities
By joining their own corporate and financial resources the municipalities intend to establish the rates for compensations paid by the citizens in such a way that these compensations can be collected and that they encourage utilization of services of waste as well as they enable necessary investments in rolling stock, equipment for recycling, treatment of disposal of waste.	By joining their own corporate and financial resources the municipalities intend to establish the rates for compensations paid by the citizens in such a way that these compensations can be collected and that they encourage utilization of services of waste as well as they enable necessary investments in rolling stock, equipment for recycling, treatment of disposal of waste.
The Joint Public Utility Company shall perform assigned tasks on disposal of solid municipal waste in such a way that they cover all of its own cost first.	Note: <i>It is not clear why this paragraph is needed in the case of Option A while not at all relevant for Option B For both option it could be considered to oblige the PUC to be cost efficient and effective in its operations to the advantage of all participating municipalities or users of the public services...</i>
Establishment of a joint public utility company, its form, activity, funds for its establishment and commencement of its operations, rights, duties and responsibilities, determining and share of profits and risk bearing, bodies and representation, et al. shall be determined later by the municipalities	Note: <i>In this case one PUC will be leading and will have a Supervisory Board and Management Board overlooking strategic decisions, while other municipalities will mainly monitor annual contract arrangements with the lead PUC.</i>

Comments:

- The agreement is mainly focused on establishment of the PUC in either form, while many aspects of future operations are to be decided later. Upon establishment allocation of capital for funding of participating municipalities to enable (re-) construction of facilities or use of new technology will be the core issue, while in a later phase the efficient functioning of the public utility for the whole territory of the region will be likely to change stakeholder relationships. This may especially be the case if strategic investors will come in on certain operations, and/or if new members (now non-participating municipalities) will join and could dilute shares of initial owner/shareholder relations.
- It is obvious that Option A is a joint effort for the longer time, while Option B is a form of contract management without much less direct management influence for the other municipalities involved.
- It is assumed that in Option A there will be more parties (shareholders) involved without one having clear dominancy (> 50 %), while in Option B the leading PUC will have a dominant share. In current practice the first one is called “a regional utility company”, while the PUC in Option B may still have “a regional function”. This shows ownership relations are still important, while for the longer run optimization of services for the region in terms of efficiency and effectiveness will more likely to be important than ownership.





Review of options for cooperation and private sector involvement

In the model contract a statement is made on regional sector policy imposing further obligations on municipalities to cooperate in a regional concept a re-assessment can be made of cooperation options.

The article 3 also opens options for private sector involvement under the condition that private companies can provide the same services at lower cost.

Comments:

- Apparently municipalities/PUC's need empowerment of sector policies to find cooperation, while such cooperation cannot be concluded based on efforts of efficiency and effectiveness alone.
- It is positive that option for private sector involvement is provided but in evaluating options municipalities should end and/or make subsidies explicit and have a cost accounting taking into account all relevant cost of the operation.

Services in waste management for municipalities not included in the agreement

This paragraph opens the possibility for participating municipalities to offer capacities to other non-participating municipalities.

Comments:

- It is not clear why this cannot be done in direct contracting with the new PUC, either in option A or option B and should be preserved though the participating municipalities.
- The question is if offering available capacities to other non-participating municipalities does not confirm gaps in efficiency and effectiveness of the PUC involved?

Decision making

A Paragraph 5 has to assure that municipalities take upon themselves to adopt uniform decisions for the whole territory.

Comments:

- This article increases transparency into obligations of the subjects of public services and shows a uniform approach into conditions to be established while also indicating a common approach to pricing of these services.
- It does not solve what pricing will be of individual municipalities in case their will be a gap with current pricing, unaccounted fees, etc.





Committee for Coordination of Cooperation

Supplemental to the Administrative Bodies required by Law a Committee for Coordination of Cooperation will be established with representatives appointed and paid by the municipalities involved.

1. The main function of such Committee will be to submit uniform proposals for the Municipal Assemblies on:
 - Draft decisions on the establishment of the either joint public utility or delegation of responsibility to a leading PUC;
 - Proposals of statutes and other general enactments to be in effect on the whole territory of all municipalities;
 - Proposal on the first director of a joint public utility company (if Option A is chosen);
 - Determining and changes of proposal of initial Business Plan of the PUC and particularly business program, plan of basic assets and systematization of positions;
 - Amendments and addenda to the agreement
 - Opinion on all issues related to contracts on performance of services in case private sector operators are involved or non-participating municipalities are offered services;
 - Provision of necessary guidelines to the municipalities for realization of cooperation activities;
 - Establishment of uniform compensations/rates and uniform conditions for service operations.
2. Proposals formulated by the Committee are obligatory in content and cannot be modified;
3. Directors of existing PUC's can attend sessions of the Committee. They shall have right to present their views on relevant topics on the agenda. They are obliged to inform Committee on all relevant issues related to that utility company;
4. The Committee will adopt Rules of Procedure for its functioning.

Comments:

- The establishment of this new body reflects the real value of the inter-municipality cooperation agreement as the function of this platform unifies participating municipalities in the preparation phase of decision making without having to involve all bodies of all municipalities at the same time. The participating municipalities have now direct influence in preparatory activities through their own representatives, while maintaining final approval of proposals of the PUC.
- It is assumed that the function of the Committee is a transitory one as the main functions of the new legal entity upon formal establishment will at a certain time take over.

Working procedures Committee

The following Articles 9, 10 and 11 of the model agreement elaborate the preparations of sessions of the Committee, the convocation of sessions and working procedures (mainly regarding in principle public sessions of the Committee unless otherwise decided).

Article 12 details the decision making of the Committee, mainly indicating that decisions can be made if half of the members are present and will be based on simple majority voting.

In case of even number of votes the President of the Committee will take the decision, unless otherwise determined in the Rules of Procedure.

Comments:

Especially Article 9 is most relevant as it details requirements of proposals made by the Committee, including providing the rationale for the proposal, providing different options and detail costing aspects of activities proposed.





Employment

Article 14 (A and B, related to the main Options A and B) are important as they arrange employment conditions for workers in the public utility companies involved.

In the case of Option A the joint public utility company will employ staff/workers and in case they will be no longer needed workers will be taken over by the participating municipalities based on their shareholding related to a ratio of inhabitants between local/regional territories.

In case workers were previously employed by a local PUC they will be taken over by that PUC.

In the case of Option B staff/workers will be employed by the leading PUC, but other municipalities /PUC's will have the preference for new jobs at the new utility company. In case these workers are no longer needed they will be taken over by the other public utility companies of the participating municipalities based on their shareholding related to a ratio of inhabitants between local/regional territories. In case workers were previously employed in one of the municipalities they will be taken over by the same utility company in that municipality

Comments:

- These articles provide practical solutions for sensitive issues concerning employment of workers of the municipalities involved.
- It is not clear why it is not envisaged in both options that participating municipalities could have a preference in appointment of staff/workers from their municipality.
- In case of termination of employment both options show no real difference as staff/ workers have the right to return to their previous public entities or work in utilities in their former municipalities. This shows the concern of local public utilities to provide employment.
- The key question is if the obligations to take workers back, in case of termination of work at the new public entity, do not limit efforts towards optimizing efficiency of all public entities involved? Why is only transfer back taken into consideration and not other acceptable options? Would it not be possible to apply retrenchment and out payment schedules for redundant personnel be linked to increased efficiency of the new utility?
- The clauses regarding return to previous work are not in any way related to the duration of the work period with the old and/or new company and reflect in principle the right on employment for workers involved apparently to smoothen decision making from the municipalities involved.

Financial issues

Article 15 specifies financing of the proposed operations and links municipality contributions to the number of inhabitants according to the last published census and to average income of the inhabitants.

Comments:

- As not in all public utilities all inhabitants of the municipality are provided with services it could also be taken into consideration to link to number of paying customers per municipality which would reflect longer term customer service and customer relationships as well.
- In the longer run financing will have to be linked to use of services in terms of ratio's of services provided (i.e. waste in kg for businesses, or waste bins per inhabitant, etc).





- In practice from current case studies can be derived that a link is made with financial contributions from the municipality involved, which may also be related to underlying inhabitant ratios. Financial ratios are very relevant as, increase of tariffs up to cost levels, decrease of unaccounted services, expanding service range, re-investments in infrastructure development are all powerful indicators for (increase of) stakeholder's value in the development of the new public utility.

Reporting

The parties involved agree in Article 16 to oblige the new utility company to make an annual report including:

- Main events, planned further development of the utility company;
- Changes in fund of land plots belonging to the company and other rights over land properties;
- Status of own capital and reserves and level of utilization of main facilities;
- Operational revenues based on statistics of amounts of funds and compensation fees/taxes;
- Personnel cost based on statistics and number of staff employed with details of total amount of incomes, social contributions, pension contributions and all other contributions in the at business year.

Comments:

- In principle the indicators requested have general importance for monitoring of the company;
- It could be considered to have more insight in financial ratios such as Return on Capital Employed (ROCE), Return on Investments (ROI) and other financial ratios. These ratios should be linked to the specific sector of public services involved.
- It could be considered to request some benchmarking of public utilities in a comparable category or comparable position to increase efforts towards efficiency and effectiveness of public utilities and give insight to decision makers to conclude on operational and financial results.

Withdrawal of municipalities and Termination of the Agreement

Withdrawal can be based on cancellation of the Agreement by the municipality or on exclusion.

Grounds for exclusion are provided, such as failure to meet obligations, serious break of obligations under the agreement and own conduct of municipalities compromising other participants.

Exclusion needs to be based on prior legal notice and need consent of all participating municipalities without veto for the municipality concerned. This municipality will be offered the opportunity to exchange its views prior to the decision. Withdrawal will be put into effect at the end of the business year.

The municipality concerned may request return of funds invested without interest obligations. The return of investments shall be based on remaining accounting value according to a scheme decided by the Committee with an optional timeframe of between 3-5 years.

Comments:

- Withdrawal or termination of agreement do not cover all aspects concerned, but merely provide a procedure and obligations to return funding with certain conditions.
- It is clear that withdrawal is made difficult as the municipality concerned will only retrieve invested funds including depreciation and excluding interest and may have to wait for max 5 years to receive funds.





- Withdrawal does however not deal with multi-year arrangements such as concession contracts or the economic effect for the project if one of the municipalities is withholding further support for the project. Suppose a project is based on a rationale of serving a number of x citizens, what if the retreating municipality takes the fundament away under the economic rationale by looking for an other way of providing services?

General Conclusion

- In practice many issues have to be addresses and elaborated in the framework for Inter-municipality Agreements, which have as a main concern to set up a feasible structure for involvement of a number of municipalities. Current solutions find their limitations in not getting really away from direct political interference and may face the continuous difficulty having to consult many municipality bodies at the same time.
- Corporatisation of public utilities can provide a new framework for newly established regional public entities and also provide a clear management structure and more rational basis of involvement of the owners and users of municipalities involved.

6.12 Institutional strengthening as covered in current grant contracts

From the viewpoint of institutional strengthening attention must be given to factors ensuring sustainability of the project as included in grant contracts for the different projects, such as:

- Policy support
- Appropriate technology
- Environmental protection measures
- Social aspects
- **Institutional and management capacity**
- Economic and financial analysis

Each of the topics is described in general as to its substance and monitoring.

Institutional and management capacity (Par. 6.5. of grant contract):

In the current grant contracts is mentioned:

- The managerial and operational capabilities of the PUC's and institutional arrangements between the Municipality and the PUC's needs to be reviewed so that the operation and maintenance of the project after implementation is carried out in an efficient manner;
- To this end MIASP will assess the institutional set up of the PUC's and suggest improvements measures, identify weaknesses and constraints in the project set-up, specify the required Organisation and Management arrangements for the project and the staffing requirements and suggest adequate action to be taken.

Reviews of the grant agreements also learn that:

- No specific targets are yet indicated and/or agreed upon.
- The elaboration of these issues could be made more specific and conditional.
- However economic and financial analysis also include specific topics which will require in some way institutional strengthening, such as full cost coverage, eliminating cross-subsidies, improving debt service ratio's, longer term adaptation of tariffs.





Conclusions:

Considerations on the current practice of application of grant contracts are:

- Determination of targets and monitoring is mainly short term aiming at qualification and approval
- After 1st year audit not much interest anymore.
- Capacity enhancement mainly focused on providing training facilities or providing training to key staff as an obligation to the project.
- Monitoring is mainly focused at finalizing (re) construction of technical facilities and control of investments/funding.
- Monitoring of institutional aspects would require a longer term effort and possibly separate funding.
- Funding of larger projects aiming at a regional approach offer the momentum to break through current forms of public administration also aiming at greater efficiency and effectiveness of the regional project beyond the existing municipal projects on a smaller scale.
- In the competition for funding of proposals efforts in the direction of higher efficiency and effectiveness of the organization of new entities could be encouraged in the qualification for donor funding. This implies that from the start improvements in efficiency and effectiveness should be given more explicit attention.

6.13 Capacity building activities as proposed by MIA

In the framework of support to communal enterprises some specific activities are proposed²⁰ for joint MIA and MIASP programmes such as developing Guidelines for PUC transformation processes in the following fields:

1. Contract Procedures within the MIA Infrastructure Projects;
2. Tender Procedures within the MIA Infrastructure Projects;
3. Core Implementation aspects of the MIA Infrastructure Projects;
4. Monitoring of the Implementation of the MIA Infrastructure Projects;
5. Improvement of Financial and Budget Management Practices in the participating municipalities;
6. Improvement of the Operational and Financial Management Practices in Public Utility Companies;
7. Public Utility Companies Transformation Guidelines.

While the first mentioned activities are core elements within MIA support especially the last four subjects would have impact on improvement of performance of communal enterprises.

For this reason some of these subjects have been elaborated in lead questions below:

Improvement of the Financial Management in Municipalities:

- How to make assessment of investment needs?
- How to make a plan of public borrowing?
- How to get into debt in order to finance local infrastructure projects using all possible instruments?

²⁰ White paper - All Capability Enhancement Aspects by Mr. Branislav Pejic, Legal Advisor MIA, June 2006





- How to finance other long-dated needs as well as short-dated needs?
- How to create system of public debt management in local units?
- How to make assessment of repayment of the principal and of the interest?
- How to make appropriate justification of the domestic account plan, its appropriations and its allocations with the account plan used within EAR Programmes?

Within the Improvement of Budget Management in Municipalities:

- How to make review of current revenues and current expenditures?
- How to make review of expected revenues from foreign and domestic loans?
- How to make assessment of new indebtedness in current budgetary year?
- How to make assessment of indebtednesses in the next budgetary year and following two budgetary years (Budget and Memorandum)?
- How to make assessment of other possible obligations for the budget?
- How to make assessment of repayment of principal and interest and their allocation in the budget?
- How to spend budget surplus?
- How to identify finance recourses for financing of the budget deficit?
- How to describe and make assessment of tax expenditures?
- How to make assessment of the permanent and current budget reserve?
- How to make a precisely difference between direct and indirect budgetary users?
- How to improve budget reporting?

Improvement of Financial Management in Public Utility Companies:

- How to make assessment of investment needs?
- How to make a plan of obtaining of the missing recourses?
- How to get into debt in order to finance infrastructure project?
- How to manage debt?
- How to make assessment of repayment of the loan?

Improvement of Operational Management in Public Utility Companies:

- How to improve availability of tariff setting?
- How to create effective enforcement policy in order to minimize non-payment of bills for delivered communal goods and services? What kind of tools to use?
- How to make savings in process of production and delivering?

Improvement of Public Utility Companies` Position and Performance:

- How to use current instruments determined by domestic positive legislation in order to improve position and operation of PUC's (entrusting of activities, join-venture arrangements, privatization, concession and other kind of public private partnerships)?
- How to determinate participation of private capital in the structure of public utilities? Which part of that capital would be acceptable in particular communal fields defined with the Law on Communal Activities?
- How to improve position and operation of PUC's in accordance with European standards.





Capacity enhancement efforts as described in the paragraphs hereafter such as training and use of FOPIP as a management tool are focused on support to the questions as mentioned in the MIA approach above.

6.14 Capacity Enhancement through training activities

This activity is covered in the recent Inception Report Municipal Infrastructure Agency Support Programme of May 2006²¹, which mentions the following activities:

Capacity Enhancement of Municipalities and PUC's	
Objectives	To enhance the capability of municipal and PUC staff in the preparation and financing of municipal infrastructure projects To ensure the proper implementation and the sustainable operation of project investments
Expected Results	Municipal and PUC staff trained on the identification and preparation of municipal infrastructure projects Municipal and PUC staff trained on the financial and budgetary aspects of project preparation and project management Municipal and PUC staff trained and acquainted with project implementation and monitoring procedures Capacity Enhancement Programs prepared and implemented in 10 PUC's to achieve sustainable financial and technical operations at the PUC level Capacity Enhancement Strategy Document for MIA aimed at improved preparation, financing and implementation of municipal infrastructure management, including a set of models to be used in the transformation of PUC's.

The activity is also covered in the recent Inception Report Municipal Infrastructure Agency Support Programme of May 2006.

<p>To achieve the project objectives and results of the Capacity Enhancement (CE) component, the MIASP will be working in close consultation with the MIA, Municipalities, their PUCs and other relevant stakeholders. The CE component will comprise the following activities:</p> <ol style="list-style-type: none"> 1. Training of Municipal and PUC Staff in; <ol style="list-style-type: none"> a. Management of Project Implementation; b. Municipal Finance and Budgeting; c. Project Identification and Preparation. 2. Improve the operational and financial performance of PUC's; 3. Preparation of guidelines for transformation of PUC's; 4. Assistance to the PUC Subotica in finalizing the Service Level Agreement (SLA) with the Municipality of Subotica.
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6.15 Financial and Operational Performance Improvement

Under the tool name FOPIP activities are undertaken towards Technical Assistance for Financial and Operational Performance Improvement, especially regarding planning instruments.

²¹ Inception Report- Municipal Infrastructure Agency Support Programme - Additional Services - Republic of Serbia
draft Report to EAR - 03SER01/11/008





The activity is also covered in the recent Inception Report Municipal Infrastructure Agency Support Programme of May 2006.

Improve Operational and Financial Performance of PUC's

We propose to carry out assessments and prepare and implement tailor made action programs for the individual PUC's in those Municipalities that have signed a grant contract. In these programs emphasis will lie on the financial performance of PUC's but also other fields of activities (e.g. technical, organizational or customer relations) may be included. A major issue will be an analysis of the tariff levels for municipal services and to develop together with the PUC's scenarios to adapt tariffs to the required levels. The following steps will be carried out:

1. Collect data and indicators of PUC performance and verify with the PUC that these data are correct;
2. Together with selected staff of the PUC assess the major problems and potential bottlenecks that may disrupt or hamper the implementation or sustainability of the project or the repayment of project loans;
3. Analyze together with PUC staff the causes of the identified problems and bottlenecks and formulate remedial actions;
4. Formulate and agree on an Action Plan that specifies the remedial actions to be undertaken by the PUC and/or the municipality and the activities in which the MIASP will provide technical assistance;
5. Implement the action plan in which the PUC will have the lead.

6.16 Elaboration of Factors ensuring sustainability of the project:

In the framework of the current grant contracts attention is given to factors ensuring sustainability of the project, indicating:

- Policy support
- Appropriate technology
- Environmental protection measures
- Social aspects
- **Institutional and management capacity**
- Economic and financial analysis

These factors are also the main attention point in the Feasibility Study for these projects.

Institutional and management capacity is one of them touching on the main theme of this report.

Institutional and management capacity (As is currently stated in Par. 6.5. of grant contract):

- The managerial and operational capabilities of the PUC's and institutional arrangements between the Municipality and the PUC's needs to be reviewed so that the operation and maintenance of the project after implementation is carried out in an efficient manner;
- To this end MIASP will assess the institutional set up of the PUC's and suggest improvements measures, identify weaknesses and constraints in the project set-up, specify the required Organisation and Management arrangements for the project and the staffing requirements and suggest adequate action to be taken





In the assessment of the current projects ²² some observations can be made:

- The focus on these aspects is mainly short term aiming at qualification for funding and approval
- After 1st year audit there is in general not much interest anymore.
- Capacity enhancement is mainly focused on providing training
- Monitoring is mainly focused at finalizing (re) construction of technical facilities and control of investments/funding.
- Monitoring of institutional aspects would require a longer term effort which may go outside the scope of throughput of ongoing projects and programs.
- However also the last mentioned topic: economic and financial analysis, covers specific topics which will require institutional strengthening, such as reaching full cost coverage, eliminating cross-subsidies, improving debt service ratio's, longer term adaptation of tariffs.

Conclusions

In the attention for strengthening Institutional and management capacity some challenges still remain:

- No specific targets are yet indicated and/or agreed upon;
- This attention point could be made more specific and conditional in the sense that elaboration of this issue in project proposals and implementation should increase eligibility for funding;
- Increased efforts for compliance and monitoring could pay off for the longer term to contribute to increased efficiency of the public utilities involved, but may require specific funding and project efforts.

6.17 Benchmarking public utilities

One of the main challenges which could have great impact on institutional strengthening is development and implementation of benchmarking. From consultant reports it is clear that many PUC's still struggle with establishment of relevant databases on public utility services. Either specific data are not available or the definition and quality of the data needs to be further addressed. From the side of KOMDEL the remark was made that in the last five years many surveys have been made to collect relevant data, but also that municipalities and PUC's have become weary for further questionnaires. KOMDEL accentuates the fact that the information provided needs further assessment to be of use in analysis and research. In practice there is much variance in application of data. In practice there are many stakeholders doing something but not all due to capacity limitations.

Also the question remains which institution seems best equipped to maintain PUC databases?

For an optimal functioning of a PUC database and/or benchmarking system it is recommendable that:

- All municipalities can or may be involved;
- Stakeholders have a clear interest in providing information, which will lead to improved return information or information which provided added value, such as generation of data at higher aggregations levels or comparisons between categories of municipalities in relevant format.
- The system must be transparent and accessible for main stakeholders.
- The ownership of a benchmarking system stays close to owners of the necessary input and output of information in the system.

²² Annex 5 Case studies of projects in relevant sectors





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- Benchmarking efforts should be intensified.

From this it is clear that the municipalities have a firm role in this, which may also be allocated to a common platform such as the Standing Conference on Towns and Municipalities (SCTM). Supplemental to these sector organizations may be involved, but this should not in any way jeopardize the ownership of such systems.

Conclusions:

- Benchmarking should play a major role in the set up and monitoring of improvement projects.
- Per sector the elaboration of methods and systems may be quite different.
- The SCTM could be appointed as a final platform to organize such databases for the longer term with support of all municipalities or at first selected municipalities which show “best practice”.
- For the start consultants/ professional associations can be involved in start up and set up design and elaborate database and systems and transfer to final destination in later phase with continuous and increased involvement SCTM and selected “best practice’ municipality staff





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ANNEX I

Terms of Reference

11-01-2007



Municipal Infrastructure Agency Support Programme
An EU-funded project managed by the European Agency for Reconstruction
9R5927/CvS/P2006_97/R001

Transformation of Public Utility Companies in the Republic of Serbia
Report



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Position: International Expert on Transformation of Public Utility Companies (PUC's).

Name of expert: Mr. Hans Kok

Duration of assignment: 40 days

Planned period of first mission: June 2006.

Background

Under the EAR sponsored Municipal Infrastructure Agency Support Programme, the Consortium, consisting of Royal Haskoning, IHS and Deloitte assists the European Agency for Reconstruction and the Municipal Infrastructure Agency in preparing technical and financial project documentation and in the monitoring of implementation of municipal infrastructure projects. The purpose of this programme is to enable municipalities and local public utility companies in the Republic of Serbia to access financial resources for creditworthy infrastructure projects.

Objective of the program

To enhance the capability of municipal and PUC staff in the preparation and financing and implementation of municipal infrastructure projects and in the sustainable operation and maintenance of project investments

Main tasks of the Expert

- Have discussions with the Management of MIA and with the EAR Program Manager on the scope and purpose of the Mission;
- Have interviews with other related Ministries (together with selected MIA/SP staff as required) on current policies and strategies with regard to the position and functioning of public utilities in Serbia;
- Interview senior municipal and PUC staff in selected Municipalities (together with selected MIA/SP staff as required);
- Review available information on PUC's in Serbia (a.o. from MIA Database)
- Review available legal and regulatory information from other relevant organizations or institutions;
- Review options for the allocation of key responsibilities for municipal service delivery;
- Review options for the further corporatization and/or private sector involvement in the municipal services sector;
- Describe organizational and managerial 'best practices' in relevant PUC's;

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- Propose an outline of MIA Guidelines for Transformation;
- Propose further activities necessary to complete the Guidelines.

The assignment will follow a phased approach:

1. Phase 1 (First mission): Identification;
2. Phase 2 (Second/Third mission): Formulation of the conclusions;
Recommendations.

Organization

The Expert will work from the MIASP office in Belgrade and under responsibility of the Team Leader of the MIASP and collaborate with other staff involved in the project. The expert will be assisted in the tasks by Serbian Local Consultants as required. The expert will collaborate closely with staff of the MIA and of municipalities and PUC's involved in the program.

Duration

The expected duration of the assignment is 2 months spread over 2-3 missions. The first mission is planned to take place in June 2006 and will have duration of approximately 3 weeks.

Deliverables and outputs

- Minutes of meetings;
- Report on the findings (facts and recommendations);
- Outline of MIA guidelines for transformation of PUC's.
- Mission report;





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ANNEX II

List of Relevant Policies and Strategies

11-01-2007



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Sector	Documents
General	<ul style="list-style-type: none"> • Inception Report - Municipal Infrastructure Agency Support Programme - Additional Services, Republic of Serbia, European Agency for Reconstruction in Belgrade, May 2006. • Strategy of Public Administration Reform in the Republic of Serbia, Ministry of Public Administration and Local Self-Government - Belgrade, 2005 • Governmental Memorandum to the Budget Law 2006 dated December 10th, 2005 • Inception Report MIASP II
PUC's	<ul style="list-style-type: none"> • Law on Public Companies and performing of activities of Common Interest (unofficial translation) • Law on changes and Amendments on the Law of Ministries, Art 7 extension art 28a with MIA, Belgrade 2003 • Paper by Mr. Branislav Pejić: Institutional Analysis of the position and affairs of a local self government unit in the Republic of Serbia and public utility companies. • Capability Enhancement MIA Proposal. • EBRD Model Service Agreement Amended 5. • FOPIP Budgeting Tool Outline, Internal document Royal Haskoning.
SCTM	<ul style="list-style-type: none"> • The Strategic Plan of the Standing Conference of Towns and Municipalities 2005 – 2008 – draft November 2004 • Report Logo East Twinning Framework Serbia, Improvement of the internal management of local governments in Serbia 2006 – 2007. • Regional waste management Plan, SCTM Regional Plan tool 11 • Establishment of Waste Transfer stations, SCTM Green Paper Tool 10.
Water supply and sewerage	<ul style="list-style-type: none"> • National Environmental Strategy of the Republic of Serbia, draft, 17 June 2005, Directorate for Environmental protection – Ministry of Science and Environment. • Water Resources Development Master Plan, Information from Ministry, Directorate of Water, Serbia 2001. • Program of construction, rehabilitation and maintenance of water management facilities in 2006 -Ministry of Agriculture, Forestry and Water-Directorate for Water • Sector Review paper on the Water Supply and Waste Water sector, Royal Haskoning - May 2006 • Global Serbian Wastewater Study, EAR – 2005 • National Environment Action Plan – EAR and Ministry of Science and Environmental Protection, 27 November 2006. (Unofficial draft) • EBRD Initial and Final Report Serbia and Montenegro: Institutional Support for the Water Utilities in Kragujevac, Nis and Novi Sad, Belgrade- May 2005 and May 2006. • Tariff concept for Nis and Novi Sad by Dr. Fromme International Consulting 2002 • Study on the Improvement of Commercial Performance of Public Municipal Enterprises for Water Supply and Sewerage as well as District Heating in Novi Sad, Niš and Belgrade by Stone & Webster Consultants – December 2001. • Aide Memoire 0406 Final (World bank water sector)
District Heating	<ul style="list-style-type: none"> • Energy Sector Development Strategy of the Republic of Serbia by 2015, Ministry of Mining and Energy, Belgrade, May 2005. • Energy Law, Official Gazette RS No 44/2004
Solid waste	<ul style="list-style-type: none"> • The National Waste Management Strategy incl. the program of harmonization with the EU, Ministry for Protection of natural resources and environment, Belgrade 2003 • GTZ brochure on PPP project in field of solid waste management with Trojon & Fischer EKO, 2006





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ANNEX III

List of relevant Laws and Regulations

11-01-2007



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1. The Constitution of the Republic of Serbia.
2. The Law on Self-Government.
3. The Law on Public Administration.
4. The Law on Public Revenues and Public Expenditures.
5. The Budgetary System Law.
6. The Law on Budget of the Republic of Serbia for 2005.
7. The Law on allocation of transfer means from the budget of the Republic of Serbia and participation of municipalities, towns and City of Belgrade in income tax in 2005.
8. The Law on securities` market and other financial instruments.
9. The Law on Tax Procedure and Tax Administration.
10. The Law on Communal Activities (Official Gazette 16/97, 42/98).
11. The Law on Public Companies and Performance of Activities of General Interest.
12. The Law on Commercial Corporations (with respect to earlier Law on Enterprises).
13. The Law on Water.
14. The Law on Solid Waste Management.
15. The Law on Environmental Protection.
16. The Law on Assets in the Ownership of the Republic of Serbia.
17. The Law on Privatization.
18. The Law on Concessions.
19. The Law on Planning and Construction.
20. The Law on Foreign Investments.
21. The European Charter on Local Self-Government of European Council.





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ANNEX IV

Overview Legal framework for central and local governments in the Republic of Serbia





Source: Prepared for European Investment Bank «Municipal Infrastructure Projects» by Branislav Pejčić, Senior Legal Adviser MIA, December 2004.

In order to determine starting base in policy of local infrastructure development in Serbia, as well as of preparing and financing projects in various fields of communal activities and infrastructure in Serbia for that purpose, it is necessary to start with some basic knowledge, and also in some cases detailed knowledge, on the most important relations, responsibilities and regulations that are valid in the legal system of the Republic of Serbia. Therefore, the analysis and list of these regulations can be treated in two ways: first, through laws and other regulations important for the system position of the municipality and public services (public institutions, public enterprises, and agencies), their rights and obligations, as well as regulated procedure (hereinafter referred to as: status and procedural regulations), and secondly, laws and other regulations whose provisions have an essential significance on the work and capabilities of the Municipal Infrastructure Agency as implemented agency in European Investment Bank projects (hereinafter referred to as: crucial regulations). Some of the regulations are listed only in one of these two groups, and some of them can be seen as belonging to both groups of regulations. The projection is presented in the form of a short overview with data on the wanted direction of changes, i.e., with the contents of new regulations (hereinafter referred to as: new regulations).

1.2 Relevant Background

Communal activities and services in Serbia are very characteristic, out of two reasons at least. The first one is that public utility companies (PUC) have a unique legal position and the second one is the lack of financial means, starting from the 1990-s and up to the present period. There are numerous consequences that resulted from these two aspects. However, those that originate from the both stand out. They are related to the deterioration of the public service quality and products that PUC-s provide in local self government units (hereinafter: municipalities), the lack of regular revenues and the inability of PUC-s and municipalities to obtain financial resources (via credits from local banks or foreign financial institutions).

The legal status of PUC-s is characteristic because, among other reasons, there are no system regulations in the field of indebtedness and credit contracts. Public Debt Law is not yet in the procedure for consideration at the competent ministries and the Government of the Republic of Serbia. The absence of these regulations and the prolongation of 'general' status of municipalities and PUC-s as it were (the old Constitution of the Republic of Serbia is still in force, as well as two system laws of this area: Law on public enterprises and activities of general interest and the Law on communal activities), led to lack of loans as additional financial source. This situation disables the core changes of the position of municipalities in the direction of strengthening its autonomy and decentralization in every sense of this word (starting with major responsibilities to the financial sustainability). The position of PUC-s in Serbia depends on the beginning of the process of core decentralization of municipalities.

1.3 Current state of affairs

Municipal finance depend on the income determined in the system of public revenues which are noted and listed in the municipal budget, while operation of PUC-s depend on the billed and collected revenues for services and products they provide. One of the basic responsibilities of the municipalities is the field of communal activities. Municipality performs these activities by establishing PUC-s or delegates them to





private enterprises or entrepreneurs. Should the communal services be delivered in an inappropriate manner, municipality is to be held responsible as well, since it is the founder of the public enterprise performing activities at the local level. This also applies to the field of water supply which is the sector constantly to be developed and enhanced as an indispensable precondition of the normal life of citizens (this area is determined in details with the Law on water). The current state of the water supply sector and other communal activities determined by the Law on communal activities, demands technological modernization of working conditions and tools (briefly they can be described as activities performed by the means of obsolete technology and which do not meet the requirements of citizens). However, the modernization calls for additional financial means which can be obtained by municipalities/PUC-s taking loans. Credits are long-termed when it comes to bigger projects of major importance, but the possibility of middle-termed or short-termed loans is not excluded, or any other legal way of financing a part of the water supply project (bonds). After these measures taken, it is reasonable to expect the rise of quality of the services as well as their tariffs, which would represent a good starting point for making PUC-s autonomous, efficient and market oriented enterprises.

2 CURRENT LEGAL FRAMEWORK

2.1 Status and Procedural Regulations

Apart from laws and other regulations regulating the status of municipality and public services, the Constitution, the highest legal act of the Republic, first defines the term municipality, and generally, its position in the Republic.

2.2 The Constitution of the Republic of Serbia (“Official Gazette of the Republic of Serbia”, No. 1/90).

Article 7 of the Constitution defines the municipality as a territorial unit where local self-government is carried out. Article 113 of the Constitution defines affairs that the municipality is in charge of through its bodies. According to this provision, the municipality:

- adopts the development programme and plan, budget and annual balance sheet;
- defines and provides for the performance of public works;
- organizes and provides for the utilization of city building land and office space;
- takes care of the construction, maintenance, and utilization of local network of roads and streets, as well as other objects of general interest;
- takes care of securing special needs of the citizens in the fields of: culture, education, health and social care, social care on children, physical education, public information, craftsmanship, tourism and services, protection and development of environmental protection, as well as other areas of immediate interest for the citizens;
- implements laws, other regulations and general acts of the Republic of Serbia for whose implementation the municipality is in charge of, provides for implementation of regulations and general acts that the municipality adopts;





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- founds bodies, organizations, and services, in order to satisfy the needs of the municipality and takes care of their organization and work;

- executes other affairs stipulated by the Constitution and law, as well as the status of the municipality.

This act regulates that the system of local self-government is regulated by special law, as well as that the Republic can entrust some affairs, and allocate some financial funds for that purpose.

2.1.2. Budgetary System Law (“Official Gazette of the Republic of Serbia”, No. 9/02 and 87/02).

Provisions of this law referring to the procedure of consideration and decision-making on the borrowing on the part of the municipality and other legal entities (which also includes public utility companies) by concluding a credit contract, i.e., granting state guarantee as defined in Articles 53 and 55. The municipality can incur debts only for the purpose of capital investments and the decision on that is made by the municipal executive body (“municipal government” while it exists, since the Law on Local Self-Government abolishes the so-called municipal government as an institution starting from the realization of local elections in autumn 2004). The municipality, in special cases, can finance a short-term deficit in the current liquidity with a short-term loan from the budget of the Republic. The municipality shall not issue a guarantee. Only the Republic can issue the guarantee. The state shall issue a sovereign guarantee on certain conditions for the debts of the municipality and other legal entities. The Government passes a decision on granting the guarantee, following a proposal of the line ministry in charge of finances. As part of the so-called crucial regulations, essential aspect of the municipal, i.e. public company’s, borrowing is considered.

2.1.3. Law on Public Enterprises and Performance of Activities of General Interest (“Official Gazette of the Republic of Serbia”, No. 25/00 and 25/02).

The Law on Public Enterprises and Performance of Activities of General Interest defines the term public enterprises and the term activities of general interest. Public enterprises are founded by the state, province, or municipality. The activities of general interest are performed by public enterprises, or other forms of organization, such as enterprises (private or joint), and entrepreneurs. The activities of general interest, under this law, apart from other listed, are: public utility activities, activities of protecting and developing the properties of general interest (waters, roads), and other activities. The system law also defines the case of all, and not only public enterprises (Law on Enterprises), that the public enterprise is the enterprise that performs the activities of general interest and is not founded by the state, i.e. local self-government unit; the activities of general interest can be performed also by other forms of enterprises set by this law, part of the enterprise, or the very entrepreneur. When speaking of the founding and business management of public enterprises, i.e., other forms of organization performing the activities of general interest, the Law on Enterprises points to the Law on Public Enterprises and the Performance of Activities of General Interest by establishing that the founding and business management of those enterprises is performed in line with the Law on Enterprises and the law that sets the conditions and ways of performing the activities of general interest. Under both mentioned laws, organs of the public enterprise are management board, supervising board and director. The statute of the public enterprise can stipulate the founding of the executive board of directors. The issue of





compensation for utilization of properties of general interest, the authority of the founder in terms of decision-making regarding the prices of public services, and other issues set by this law as well as by the law regulating public utility activities is found in the section “Crucial Regulations”.

2.1.4. Law on Resources in the Ownership of the Republic of Serbia (“Official Gazette of the Republic of Serbia”, No. 53/95, 3/96, 54/96, 32/97 and 44/99).

The Law on Resources in the Ownership of the Republic of Serbia, on the basis of the municipality’s position set in the Constitution, as well as public enterprises, and other public services, establishes the rights, i.e., commitments, of the municipality and public enterprises in relation to means in the ownership of the state, which are thus defined by this law. The state resources are natural resources (land, waters, and other natural resources), and properties in general use (public roads and streets, and other properties in general use), objects built or acquired thanks to resources in state possession (buildings and other objects, equipment, instruments of labour), and other means used by state and municipal organs and public services. In compliance with that, regarding the immovable property used by municipalities, the Government of the Republic of Serbia makes a decision on the acquisition and alienation (sale) of immovable property while the authorized municipal organ, in agreement with the Republic Property Directorate, makes a decision on utilization or taking out a lease and taking out the mortgage on immovable property used by the municipality or public utility company (which is important in case of direct lending from banks to PUC-s) As for the immovable property used by public enterprises and other public services, the Government of the Republic of Serbia makes a decision on the alienation of immovable property while the authorized municipal administration, in agreement with the Republic Property Directorate, makes a decision on utilization or taking out a lease. The Government can make a decision that some of the immovable property that is not in function of fulfilling municipality’s actions, i.e., activities of the public enterprise, be taken away from the user.

This Law sets the possibility of acquiring concessions on properties of general interest. These provisions of the Law are discussed in the part where the framework for the so-called Crucial Regulations is given. The Law, in any case, should be subject to examination and be part of New Regulations, since the basic idea of the Law is to get adjusted to new solutions that should not be based, when resources of municipalities and public enterprises are in question, on the regime of state property, i.e. means identified as resources in the ownership of the Republic.

2.1.5. Law on Public Administration (“Official Gazette of the Republic of Serbia”, No. 20/92, 212/92, 48/93, 53/93, 67/93, 48/94 and 49/99).

The Law on Public Administration includes system provisions relative to affairs of the public administration and authorities for their performance. The affairs of the public administration are performed by ministries and separate organizations (MIA is the separate organization) while province’s and municipal organs perform certain affairs of public administration as entrusted by the law. The public administration affairs are done also by public utility companies and other kind of public enterprises, institutions, and other public services and organizations as entrusted by the law as the so-called management powers (which represent the narrower term from the so-called public legal authorization).





2.1.6. Rulebook of the Government of the Republic of Serbia (“Official Gazette of the Republic of Serbia”, No. 6/02 and 12/02).

Either in the case that the Government adopts a decision on sovereign guarantee or bill on sovereign guarantee set by the Government and sent to the Parliament for adoption, the procedure set by this Rule Book must be respected. The procedure means that before sending the general act in the form of a bill to the Government, i.e., before Government’s committees makes a statement, the authorized legislator must acquire, under certain conditions, an opinion by the Republican Secretariat for the Judiciary, Ministry of Finance, as well as Republican Public Defender’s Office.

2.2 Crucial Regulations

2.2.1. Law on Local Self-Government (“Official Gazette of the Republic of Serbia”, No. 9/02).

Articles 78, 98, 99 and 100 define primary sources, transferred revenues, and supplementary funds. Primary public sources are: the municipal administrative taxes; the local communal taxes; the residence tax; the charges levied for utilization of building land; the charges levied for utilization of urban building land; the charges levied for utilization of natural medicinal factor; the revenues from taking out a lease, i.e., taking out immovable state-owned property for utilization by the municipality and public service founded by the municipality; the revenues procured from the concession charges for the performance of communal activities, and the revenues procured from other concession affairs concluded by the municipality; the revenues procured from the interest on municipal funds; the fines pronounced pursuant to legal proceedings for offences against the municipal regulations as well as property ownership profits confiscated as the result of such proceedings; the revenue realized by municipal organs, services and organizations; voluntary financial contribution for the territory of the municipality; the revenue procured on the basis of donations; other local public revenues, in compliance with the law. Transferred public revenues are: tax on the citizens’ income (part of income tax, taxes on revenues from agriculture and forest exploitation, the revenues from independent activities, the revenues from real estates, the revenues from renting movable property, the gain from games of chance, revenues from personal insurance, the so-called other revenues levied in conformity with the income tax); the tax on the fund of gain at the rate of 3.5 percent that was abolished starting with July 2004; the tax on property; the tax on inheritance and gift; tax on transfer of absolute rights; part of the sales tax on goods and services determined by a special law (the so-called limited transferred revenues) excluding sales tax on goods realized in importing, 8 percent of the sales tax levied in the territory of the municipality, 10 percent of the sales tax realized in the territory of the city and 15 percent of the sales tax realized in the territory of the City of Belgrade (the so-called unlimited transferred revenues), noting that the sales tax on goods and services shall be void as tax form starting from January 2005, when the value added tax (VAT) shall be introduced; charges levied for utilization of goods of general interest; charges for the environmental actions; charges collected in the sale of capital in the privatization procedure. Appropriate, belonging part of the income tax and the sales tax on goods and services is set by a special, annual law. This year, a law that would regulate first six months of financing affairs in the municipalities in the manner that thus far regulated the annual participation in the realized revenue from taxes will be adopted this year. That means that during another six months, transfers from the budget of the Republic to municipalities shall be realized, after the tax on fund of gain and sales tax on goods and services shall become void. In the case that the municipality does not collect funds set on the basis of annual scope of funds (from the annual legislation), the municipality is granted supplementary funds in the proportion of the quantity of collected revenues in the budget of the Republic. The fact that some municipality shall be granted





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supplementary funds from the Republic budget is also of significance for establishing fiscal sustainability and assessment of the financial situation in the municipality.

2.2.2. Law on Communal Activities (“Official Gazette of the Republic of Serbia”, No. 16/97 and 42/98).

The local self-administration regulates and provides for the conditions for the performance of public works. The public works, in the sense of this legislation, are activities of general interest and include the activities of producing and delivering public utility products and providing public services that represent an irreplaceable condition of life and work. The activities are: filtration and distribution of water; the filtrating and diverting atmospheric and sewerage waters; steam and hot water production and supply; transportation of passengers in the public transportation; keeping the city clean; keeping and maintaining parks; maintenance of streets, roads, and other public areas and public lightening; maintenance of depots; maintenance of cemeteries and burial management. This law offers the possibility to the municipality to set other activities of local interest as public works (e.g. maintaining public parking lots, marketplaces, public bathhouses, etc.). In order to perform public works, the municipality founds public enterprises or entrusts other enterprises, i.e. entrepreneurs, to be in charge of public works. The very public enterprise can entrust certain tasks to other enterprise or entrepreneur, in accordance with the municipality’s regulation. Filtration and distribution of water, filtration, and the diverting of sewerage waters, steam and hot water production and supply, as well as tram and trolley-bus public transportation are activities performed only by public utility companies. However, if the founding of one public enterprise would not be rational having in mind the scope of activities and the number of users, the municipality can entrust these activities to someone else! Entrusting public utility activities is set on a period of up to five years, and in case the entrusting is set for the subject that takes over the obligation of investing the funds, the entrusting lasts as long as the repayment period of the invested means lasts, but not longer than 25 years. The means for the performance and development of public utility activities are allocated from the revenue coming from the sale of public utility products and services and partly from compensations for maintenance and utilization of construction land, voluntary contribution, and other legally possible sources.

The performance of public utility activities can be organized for two or more municipalities, in which case the municipalities regulate their internal rights and commitments in an agreement.

2.2.3. Law on Public Enterprises and Performance of Activities of General Interest (“Official Gazette of the Republic of Serbia”, No. 25/00 and 25/02).

In order to secure the protection of general interest in a public enterprise, i.e., in order to perform an activity of general interest, the municipality agrees to a tariff – the price list of products and services. The municipality also agrees to the public enterprise’s statute, the disposition with the enterprise’s property, act on general conditions for the delivery of products and services, investment of capital, status changes. The municipality must also give consent to the schedule of rates of products and services for the activities of general interest performed by other forms of enterprises and entrepreneurs, as well as to the statute and other decisions in line with the law. In case of disorder of business management of a public enterprise, the municipality can change internal organization of the public enterprise founded by the municipality, to release from duty the appointed officials and to appoint interim management of the enterprise, to limit the right of disposition with certain state-owned funds used by the public enterprise, as well as to undertake other measures.





Public utility public enterprises that use public properties of general interest in the performance of activities of general interest are obliged to pay compensation for using those public properties. On the other hand, public utility public enterprises have the right to invest capital in other corporations in order to perform the activities of general interest, but also the activities that are not of general interest according to the previously given consent of the municipality.

2.2.4. Budgetary System Law (“Official Gazette of the Republic of Serbia”, No. 9/02 and 87/02).

Provisions of Articles 52 and 60 regulate the debts and guarantees of the state, municipality and other legal entities. Article 54 is deleted by changing and amending the Law (“Official Gazette of the Republic of Serbia”, No. 87/2002). Municipalities can incur debts in order to finance capital investment expenditure, in compliance with the criteria set by the Government. The amount of the borrowing shall be in compliance with the capabilities of the municipality to finance the repayment of principal and interest from its own revenues. Should deficits occur in the current liquidity, the financing of municipal functions shall be made by borrowing from the Republic Budget, in compliance with the criteria established by the Government, and which have to be repaid in the Republic Budget by November 30 of the current year. At the same time, the total amount, either for short-term borrowing or long-term borrowing for capital investments) shall not exceed amount equal to 20 percent of the total realized revenues of municipality in the previous fiscal year’s budget. The question posed here, and to which there is a partial answer from the ministry in charge of finances and economy, is whether the amount of total borrowing refers to the total debt based on the principal or the total liabilities based on the total debt (principal, interest, and other expenses) during the year when the borrowing was made, as well as whether the term “total realized revenues” includes revenues realized on all bases or only on the so-called current (operational) revenues. The Republic budget defines the limit of the total amount of the guarantee for the purpose of possible guarantees in the future. The Government makes a decision on the guarantee.

2.2.5. Law on Resources in the Ownership of the Republic of Serbia (“Official Gazette of the Republic of Serbia”, No. 53/95, 3/96, 54/96, 32/97 and 44/99).

Under Article 8b of this Law, the Government of the Republic of Serbia may confiscate immovable property which is not in the function of carrying out authorities of municipal administration or activities of public companies. The Government may take away the immovable property used by other company or entrepreneur to whom the municipality had entrusted the performance of activities of general interest. The Government may take away immovable property from the above-mentioned also for the purpose of establishing a concession, in compliance with the law regulating concessions, the object of concession and the concession granting procedure. Provisions of this law, referring to concessions, should be seen together with the provisions of the Law on Public Works in the part that regulates the possibility of entrusting the performance of these activities to other enterprises (not only public companies) and entrepreneurs, as well as provisions of the very Law on Concessions.

2.2.6. Law on Concessions (“Official Gazette of the Republic of Serbia”, No. 55/03).

Under the Law on Concessions, the concession is defined in three ways, namely, as the right to utilize natural resources and resources of general interest, as the performance of activities of general interest, and as concession in accordance with the B.O.T. (built-operate-transfer) system. The concession (right to utilize, perform activities or B.O.T. concession) is granted to a domestic or foreign person, for a set





period of time, upon the payment of a concession fee and under terms prescribed by this law. The terms refer to fulfilment of terms as set by this law, concession act and public tender. An object of concession is established in 16 points as is: constructing, renovating, maintaining and utilizing the water supply facilities, water supply and distribution; construction (or reconstruction), maintenance and utilization of local roads; constructing, maintaining and utilizing the power-generating and heating facilities; constructing, maintaining and utilizing the public utility facilities intended for rendering the public utility services. A concession may be granted for a period of up to 30 years. The concession granting procedure begins in the competent ministry or the municipality on whose territory the object of concession is located, after which a proposal for concession granting is submitted to the Government. Other interested person can submit an initiative to the Government as well. The Government shall make a decision in the period of up to four months after the proposal for concession granting is submitted. A municipality prepares the final proposal for passing the concession act aimed at performing public works. Along with an opinion from the line ministry, the proposal is sent to the Government. The Government passes the Act on Concession, under the previously organized procedure of public tender. An announcement on this shall be published in the “Official Gazette of the Republic of Serbia” and one of domestic newspapers. The concession contract whose object is construction of communal objects in order to perform public works is concluded by a concessionaire and authorized organ of the municipality, with the previously given written consent of the Government. After concession granting, the concessionaire founds a “concessionary” enterprise, except in the case if the concessionaire already has a registered enterprise for performing the relating activity. All revenues collected from the concession charge for the performance of communal activities represent the income in the municipal budget.

Only in the case that concession whose subject has strategic importance for the Republic or international importance, the decision-making on granting concessions is not completed in the Government, but the Government submits the proposal to the National Assembly. Public utility activities, therefore, do not belong to the group of such cases, since their development and promotion are not among activities of strategic importance for the state as a whole. A concession cannot be granted to a foreign entity for the activities and the territory where, in accordance with the law regulating foreign investment, a foreign entity cannot establish a company. The law separately defines cases when the concession contract is broken, i.e. when the concession contract becomes void.

2.2.7. Law on Foreign Investments (“Official Gazette of the Federal Republic of Yugoslavia”, No. 3/02 and 5/03).

Under this law, a foreign national may not establish a company for the manufacture and trade of weapons nor in an area specified as a restricted zone. In any other field there is possible to establish new enterprise or to invest in existing one.

2.2.8. Law on Planning and Construction (“Official Gazette of the Republic of Serbia”, No. 47/03).

Under the Law on Planning and Construction, the objects that are built on the basis of building licence according to technical documentation for object building. The documentation includes general project, preliminary design project, main project, contracting works and the performed project. The municipality issues a grant for object building, except for the objects for which the law stipulates that the grant is issued by the province, i.e., the Republic (Republic ministry – in areas that are by nature close to public





utilities, the ministry issues the licence, e.g. for inter-regional and regional objects of water supply and sewerage system, city systems for water supply and channelling waste waters, as well as facilities for filtration of waters). The building licence is issued after a decision, in the period of 15 days from the day of application for granting the building licence. The building licence becomes void in case the object is not built, i.e., in case the construction works do not begin, in the period of two years from the day of coming into force of the building licence. The investor is obliged to inform the administration in charge of granting the building licence on the name of the constructor, the beginning of constructing works, and the closing date of construction, eight days prior to beginning of the construction works. The authorized administration is obliged to confirm the acceptance of the documentation within eight days from the documentation submission. The object built in line with regulations can be used by previously acquired utilization licence. The administration authorized to issue a building licence issues the needed licence within seven days from the day of acceptance of the report of the commission, which confirms that the object is suitable for use.

2.2.9. Public Procurement Act (“Official Gazette of the Republic of Serbia”, No. 39/02, 34/03 and 55/04).

In compliance with this law, public procurement of works is the execution of works, design and execution of works connected to specific activities set by this law, as well as the work in the course of building and civil engineering, taken as a whole, which fulfils all economic and technical requirements of the contractor. The Chamber of Commerce of the Republic of Serbia, following a public invitation, concludes a list of interested contractors of construction works, paying attention that if there is a concluded agreement with some other country, the list of contractors shall include contractors whose seat is in that other country. The contract on public procurement of services through open competition is awarded, among other sectors, to the sector of construction and civil engineering. In the water management sector, in compliance with this law, public procurements are procurement whose subject is the supply or operation of permanent networks intended for the provision of public services related to the production, transfer or distribution of drinking water, as well as the delivery of drinking water to such networks. Provisions of this law shall not be applied on public procurements in the water management sector in the case of services given by the contractor to a joint company, founded by several contractors with the aim of performing activities in the sector of the supply and management of permanent networks, for securing public services in connection to production, transfer and distribution of drinking water or drinking water distribution. If the tenderer's offer products originating from the countries with which the State Union of Serbia and Montenegro has not concluded an agreement that would provide domestic producers with an equal access on the market of that other country, such tender may be rejected, where the proportion of the products originating from that other country exceeds 50 percent of the total value of the offered product. But, above all, one should have in mind the basic provisions of the Law that generally regulate the cases where the Law is not applied. Such case is the procurement under international agreement covering the delivery of goods, performance of works, providing services or public design contests which are intended for joint implementation or exploitation of a project by the countries or organizations which concluded such agreement.

2.2.10. Law on Water (“Official Gazette of the Republic of Serbia”, No. 46/91, 53/93, 54/96, 67/93 and 48/94).

This law regulates protection of water, protection from harmful effects of water, water usage and manage, conditions and manner of water supply operating, organizing and financing of water supply and other activities related to water, as well as supervising of this law enforcement.





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ANNEX V

Relevant stakeholders and projects identified in the water sector

11-01-2007



Municipal Infrastructure Agency Support Programme
An EU-funded project managed by the European Agency for Reconstruction
9R5927/CvS/P2006_97/R001

Transformation of Public Utility Companies in the Republic of Serbia
Report



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EBRD

The cities of Kragujevac, Niš, and Novi Sad have received loans from the European Bank for Reconstruction and Development to finance priority investment programmes for the water supply and sanitation infrastructure²³. The local municipal water supply and sanitation utility companies: JKP Vodovod i Kanalizacija (Kragujevac), JKP Naissus (Niš), and JKP Vodovod i Kanalizacija (Novi Sad), are the executing agencies for the Projects.

The objectives of the consultancy services in connection with the current project are two-fold:

- to introduce Service Agreements between the Cities and the Utilities to regulate the water supply and sewerage services; and
- to help establish procedures and systems to enable the Utilities to monitor and comply with the criteria as defined in the Service Agreements.

For the Utilities these undertakings include:

- to introduce a service agreement (the "Service Agreement"),
- to carry out a programme to develop their managerial and operational practice and procedures to achieve efficiency gains (the Financial and Operational Performance Improvement Programme, or the "FOPIP");
- to adopt and implement an Environmental Action Plan ("EAP");
- to adopt a tariff policy that moves towards full cost recovery within a time-frame to be agreed with the Bank;
- to generate sufficient funds to cover its recurrent costs and maintain a debt service cover ratio of at least 1.3;
- to introduce an accounting system based on IAS and a computerised MIS system;
- to reduce their accounts receivables;
- to increase their revenue collection ratios, including cash collection.

The Problem analysis has indicated common problems to all cities involved in the program:

- No long term planning with regard to service goals, actions (investments) to meet service goals
- No long term tariff planning;
- Little internal monitoring of performance on the part of the water companies and no systematic collection of management data/performance indicators to track performance;
- Little involvement on the part of city administrations in exercising their role as regulator and monitoring utility performance.

One of the main deliverables in the project has been drafting a generic service agreement and service agreement guidelines for application and elaboration of the agreements.

²³ EBRD Initial and Final Report Serbia and Montenegro: Institutional Support for the Water Utilities in Kragujevac, Nis and Novi Sad, Belgrade- May 2005 and May 2006.





The Guidelines document provides:

- Performance indicator definitions and calculation methodology
- Methodology for defining Incentive Compensation
- Description of utility reporting requirements and examples for reporting formats (business plans and other reports including Environmental Action Plans)

A requirement of the Service Agreement will be elaboration by the utility of an annual “Service Provider Performance Report” to the Owner. This report will summarise the utility’s performance against performance indicators and targets.

For the analysis of challenges ahead in transformation of practices in utility companies the EBRD project provides important “lessons learned”

Implementation of Service Agreements requires the political will of City governments. It is necessary for City governments to see Service Agreements as a useful management/regulatory tool in monitoring water sector service performance and ensuring performance improvements.

This political will was unfortunately not present during the implementation period of the current project. It is the Consultant’s impression that stakeholders understood the potential usefulness of Agreements, but implementation was impeded by a number of factors, including:

- Lack of prioritisation on the part of City Government. Failure of the cities to designate representatives with decision making authority in the process of Service Agreement elaboration/implementation;
- Related to the above, lack of clarity among city representatives designated as to the political priorities of top leadership. This was particularly a problem in Kragujevac and Novi Sad where it was not possible to receive a definitive answer as to whether the cities were interested in participating in the project;
- A prevailing view that the Service Agreements impose additional administrative/regulatory costs;
- View on behalf of cities/utilities that existing legislation defines relationship between the parties and that changes to the Law on Public Utilities renders Service Agreements in-applicable.

The current generic service agreement can serve as a starting point for Serbian municipalities in this process. The Agreements demonstrate the level of detail needed in definition of roles and responsibilities for contract parties, relevant performance standards for monitoring service provider performance, and necessary level of reporting to be provided by service providers to city level regulators.

In the framework of the projects a separate consultancy was implemented to develop a tariff concept²⁴ for the cities involved. Interesting is the gap analysis in coverage of operations cost and total cost. Most municipalities are underway to cover operational costs, but have still a way to go to cover not only operational cost but all costs including cost of capital, depreciation and cost of capital for investments to be done urgently.

In general the projects aim at:

²⁴ Tariff concept for Niš and Novi Sad by Dr. Fromme International Consulting 2002





- Reaching full cost coverage in a certain period of time
- A gradual increase of tariffs to realize this situation.

In a recent budget indication ²⁵ the increase of tariffs for public services within PUC's in Serbia was restricted to 9, 3 %, below the level of annual inflation in the country in that year. The funding institutions European Agency for Reconstruction (EAR), European Bank for Reconstruction and Development (EBRD) and KfW have expressed their concern in order to allow the communal utilities to gradually increase their tariffs to achieve cost coverage in the medium term.

“An important condition for our engagement is always, that the communal utilities we are working together have sufficient income to sustainably maintain and operate the financed new and rehabilitated systems. If minimum cost coverage generated by tariff income is not assured in medium terms, further funding from our side can no longer be justified.

Although some communal utilities have made significant progress in the last years, tariffs of many Serbian communal utilities are still far away from allowing cost coverage. Tariffs for communal services in Serbia are now one of the lowest in whole South-Eastern Europe. Consequently, systems cannot be maintained adequately and will further deteriorate.”

In a interview²⁶ with the responsible staff of units within the ministry of Finance was highlighted that a restricted increase contributes to the increase of efficiency in the public utilities in the country.

This ongoing discussion highlights ongoing efforts of main stakeholders to balance increase of tariffs on public services with increase of efficiency in public services as one of the major concerns for the near future.

KfW Institutional support program in water sector in 4 main cities

After a, first and second phase, of support of projects for Novi Sad, Nis, Kragujevac and Belgrade²⁷ in order to upgrade water supply and sewerage systems²⁸, a third phase project has now started for institutional support to all 4 cities.

The focus of the program will be to support the four utilities to improve management systems for better operational and commercial efficiency and to explore opportunities for better revenues with more appropriate tariff systems.

The **main problems** identifies are:

- Lost revenues
- No accurate billing
- Level of operating costs
- Prioritizing maintenance activities
- Needed improvements in the billing system

²⁵ Governmental Memorandum to the Budget Law 2006 dated December 10th, 2005

²⁶ Interview June 20, 2006 with Mrs Misela Nikolic, Assistant Director Treasury Administration Public Enterprises and State Aid Division.

²⁷ Study on the Improvement of Commercial Performance of Public Municipal Enterprises for Water Supply and Sewerage as well as District Heating in Novi Sad, Niš and Belgrade by Stone & Webster Consultants – December 2001.

²⁸ Interview June 30, 2006 with Mr Alan Eaton, Team leader Institutional Support KfW project Rehabilitation Urban Water Supply and Sewerage systems in Novi Sad, Kragujevac, Niš and Belgrade.





Specifically the project shall comprise **three work packages** as the major lines of activity:

1. Asset Management: assist in efficient asset management systems and support its application in daily practice;
2. Operational and Financial Controlling: assist in controlling procedures to improve the income stream and reduce cost of collection
3. Tariff study: Conduct a tariff study in each of the four locations in order to determine the scope for adjustments of the current tariff systems with a view to improve revenue generation

The first period is review of Utility practices in 5 different areas, such as:

- Financial
- Commercial
- Operations and Maintenance
- Design and Planning
- IT and GIS

Currently the project is still in the Inception phase with reporting to be expected at the end of September 2006.

Serbia and Montenegro Waterworks Association (SMWA)

The SMWA is a professional association established to provide support to water utilities in the country. Currently a total of 59 water utilities participate in the activities of the Association, which undertakes activities in the field of research, customer surveys, consultation and technical support projects.

One of the main priority projects now is setting up a program for **monitoring of performance indicators and benchmarking** the water supply and waste water sector in Serbia²⁹.

The water management utilities are seen as the main beneficiary of the project, also contributing to raising awareness and more support of their owners the municipalities. The Water Directorate of the Ministry is seen as the first responsible for setting up performance measuring and benchmarking, while the projects has to be a joint efforts through the Standing Conference on Towns and Municipalities (SCTM) with technical assistance from the SMWA.

The problems identified are taken form best practice monitoring institutions in the water sector and the system should establish a database to be of use for all water utilities.

In the framework of the project a first phase is aiming at establishing a monitoring unit which will deploy efforts in data collection. In the second phase a responsible body should be established as a consultation platform for all stakeholders. Although main stakeholders are identified and funding is tried to be set up the initiative is not yet part of a fully approved operating system by all stakeholders.

²⁹ Interview June 23, 2006 with Mr. Milorad Rosic, Executive Director of SMWA.





However through the participation of the Standing Conference on Towns and Municipalities (SCTM) a consultation platform is established between interested parties in the development of the project, which could later be institutionalized.

Institute for the development of water sources “Jaroslav Cerni”

The Institute for the development of water resources "JAROSLAV ČERNI"³⁰ is a central non-government institution for research, development, design and consultancy in the fields of hydraulic engineering and water management. Established in 1947, the Institute was named in the honour of its first director, distinguished hydraulic engineer. During more than 50 years of its activity, the Institute has grown into the largest and leading organization in water domain in Yugoslavia.

The Institute has scientific, technical and practical experience and staff capable to cover all aspects and problems relating to water use, water protection and protection against harmful water effects. Now, the Institute employs 164 associates. More than half are professional engineers, specialists in different fields. Many of them have high academic degrees.

The professional activity of the Institute involves a range of problems, projects, services in the entire field of water resources management, from basic and applied studies and investigations, through water master planning, feasibility and detailed designs to complex multidisciplinary projects.

Being involved in many different and complex problems in Yugoslavia and abroad, the specialists and experts of the Institute has been obliged to keep abreast with the most advanced methods, techniques technologies of research, design and construction. At the same time, they have developed new approaches and methods. Many of these methods, experimental and in-situ measuring procedures and equipment, had found successful and wide implementation. At present, highly sophisticated models for wide range of system analysis, planning and management of water resources systems, are in every day practice.

The Institute took an active part in the design and implementation of almost all major water resources development projects in former Yugoslavia and FR Yugoslavia. Some of them are:

- the Djerdap (Iron Gate) Hydropower and Navigation System on the Danube River
- the Danube - Tisa - Danube Drainage Irrigation and Navigation System
- the large and medium hydropower projects: Jablanica; Zvornik; Vrutok; Vinodol; Dubrovnik; Rama; Bajina Bašta; Vlasina; Globočica; Grančarevo; Grabovica; Salakovac; Uvac; Piva; Višegrad, etc.
- the multi-purpose reservoirs projects: Vrutci; Gruza; Barje; Celije; Grliste, etc.
- the river engineering projects: the Danube, Sava, Drava, Drina, Vardar, Morava and many other rivers

³⁰ Web site <http://www.icerni.co.yu/english/vos.htm>





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- the municipal water supply systems of Belgrade, Niš, Novi Sad, Kragujevac, Kruševac, Kraljevo, Užice, Čačak, Trstenik, Aleksinac, Šabac and many other towns and region
- the sewerage and waste water treatment system of Belgrade, Niš, Zrenjanin, Trstenik, etc.
- the solid waste management strategy for Belgrade, Jagodina, Bjeljina, Brčko, etc.
- port and harbour projects on the Adriatic coast: Bar; Lora; Split; Ploče; Hvar and on the Danube and Sava rivers: Belgrade, Novi Sad, Smederevo, etc.





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ANNEX VI

Institutions involved in restructuring of local public utilities companies

11-01-2007



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9R5927/CvS/P2006_97/R001

Transformation of Public Utility Companies in the Republic of Serbia
Report



In this chapter we identify and discuss some main stakeholders in the Republic of Serbia currently involved in transformation of municipalities and public utility companies at local levels. The main focus is on the municipalities but indirectly attention is given to the public utilities as these are the main channel of service provision to the citizens.

Standing Conference on Towns and Municipalities (SCTM)

All local self-government units in the Republic of Serbia are voluntarily participating in the Standing Conference on Towns and Municipalities, which serves as a Professional Association uniting and supporting all members: the municipalities in the country. The members pay an annual fee related to their size and budget. Only 14 % of the SCTM budget is covered by this annual contribution, while the other 86 % is funded by international donor agencies³¹. Development of a professional management culture within municipalities is complicated by the fact that municipalities are influenced by and closely related to local politics, which make it more difficult for them to undertake less popular longer term decisions for the citizens of the local community. SCTM structures are aiming at raising awareness to establish common approaches based on best practice for the participating municipalities.

From the side of the SCTM the development of Business Plans for the municipalities is seen as a major step forward as municipalities are invited and enabled to plan 4 years ahead, which allows them to consider longer term options for improvement of municipal services.

The SCTM has an advocacy role supported by training and development seminars to raise awareness with municipal administrations which options are available for increasing private sector involvement, such as for example establishing Public-Private partnership (PPP) projects.

There is no database of such projects, but few examples in some municipalities such as the GTZ project with solid waste partnerships in local communities which did not do such activity before.

No examples are yet known about current activities, which have been transformed into full private sector involvement.

As changes in the Constitution and review of the Privatization program may have effect in the near future it is expected that from 2007 onwards more municipalities will be more involved in such PPP programmes or outsourcing of municipal services to private sector companies.

SCTM has approved a **Strategic Master Plan**³² for the period 2005 – 2008 aiming at 3 strategic member oriented objectives:

³¹ Interview date 26 June 2006 with Mr. Miodrag Gluscevic of the SCTM

³² Strategic Plan 2005 – 2008 of The Standing Conference of Towns and Municipalities , XXXIV General Assembly Belgrade, December 14th and 15th 2004





1. Development of representation and the advocacy role of the municipalities.
2. Development of services to member municipalities.
3. Support in Communications and Public Relations.

Supplemental to this other objectives are;

- Financial sustainability/institutional strengthening of SCTM
- Cooperation

SCTM has developed a SWOT analysis, which after consultation of its members was fine tuned as indicated in the next overview.

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Standing Conference on Towns and Municipalities (SCTM)

<p>Strengths</p> <ul style="list-style-type: none"> • SCTM Organisational structure, adequate to its role and needs of its members • Experience, high professional level of staff, SOP's available. • Nationally and internationally SCTM is well-known and recognized. 	<p>Weaknesses</p> <ul style="list-style-type: none"> • Insufficient financial sustainability and organisational stability. • Difficult relationship with Central Government. • Insufficient level of involvement of members, exchange of information and service provision.
<p>Opportunities</p> <ul style="list-style-type: none"> • Growing membership involvement and high expectations of SCTM. • International co-operation and donor support. • Ongoing process of local self-government reforms. 	<p>Threats</p> <ul style="list-style-type: none"> • Decentralisation and democratisation process slowing down; political instability. • High level of donor dependency. • One-way relations with/from CG, lack of readiness at Central Government level to cooperate with SCTM; communication structures not institutionalised.

thinking in all dimensions

Currently SCTM is giving efforts to implement the Strategic Plan, but it limited in human and financial resources to implement according to planning schedules in the Plan.

The SCTM is stimulating transfer of knowledge to municipalities with information on ongoing projects and lessons to be learned to the benefit of all municipalities, such as for instance a green paper on the establishment of Waste transfer stations³³ and a regional planning tool on set up of a Waste Management Plan³⁴.

³³ Establishment of Waste Transfer stations, SCTM Green Paper Tool 10.

³⁴ Regional waste management Plan, SCTM Regional Plan tool 11





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Privatization Agency

The Privatization Agency is the central operative institution of the concept of privatization in Serbia, and is responsible for authorising, organising, implementing and controlling the procedures of privatization. Its status, activity, administration, organisation, management and financing are defined, accordingly.

In keeping with the provisions of the Law on Privatization and according to the description of the tasks that are within the authority of the Agency, all the Agency's activities can be categorised into two basic processes³⁵:

1. Privatization and
2. Control of the procedures of privatization and execution of the contract on sale

Based on the Law of Privatization of 2005 the first phase has concentrated on privatization of enterprises at national level.

No decisions have been taken for the enterprises at local level³⁶, which has still to be decided by the ministries involved. We have been informed that the Ministry of Economy is working on policy on privatization at local levels, but at this stage no further information or exchange of ideas could be realised.

Serbia Local Government Reform Program (SLGRP) by USAID

The Serbia Local Government Reform Program (SLGRP) is designed to revitalize the deep roots of strong community based management from within Serbian society in order to re-establish an effective, responsive and accountable local government tradition. The U.S Agency for International Development (USAID) has contracted with Development Alternatives, Inc. (DAI) to implement the SLGRP.

The main objective of the program is to help local governments once again become more effective, responsive, and accountable.

USAID started the SLGRP in October, 2001³⁷. This 5-year program, funded at \$30 million, is designed to work at the local level in 70 Serbian municipalities, as well as in the City of Belgrade and its 12 constituent municipalities over the life of the program to improve municipal management and capacity in the following areas: Citizen Participation, Information Technology, Financial Management, Communal Enterprise Management and Public Procurement. It is also working at the national level to support the institutional development of the National municipal association (the "Standing Conference of Towns and Municipalities") and to support policy reform, specifically in the area of government decentralization.

³⁵ Web site <http://www.priv.yu/>

³⁶ Interview June 20, 2006 with Mr. Branislav Zec, Director and Veselinka Cuk, Project Manager Privatization Agency

³⁷ Web site SLGRP USAID <http://www.slgrp.usaid.org.yu/>





Then SLGRP support program is build around 7 key elements:

- **Public Procurement**
 - Public Procurement Team was established by SLGRP focusing on procedures and structures to create more accountable and transparent procurement and stewardship practice in the management of public resources. This additional initiative was made in response to adoption of the Public Procurement Law as well as widespread consensus on the significant impact of corruption at the interface of government and private sector in Serbia. The new Public Procurement Team works closely with the Policy Reform and Financial Management Teams to intervene at both the municipal government level and republic government level.
 - A training curriculum, featuring a "Basic Public Procurement Course" and several "sub-courses" will be developed by the SLGRP Procurement Team with the input and assistance of selected local and regional experts. The Public Procurement Team will subsequently participate in training events - especially initial training of other trainers - but also in "Basic Course" and "Short-course" events; monitor all training; and develop new or amend existing training courses as the need arises. Beginning soon after the "Basic Public Procurement Course" has been offered to municipal procurement staff; the Procurement Team will provide on-site support to municipal procurement workers and offices and will conduct surveys for measures of effectiveness.

- **Financial management**
 - The logic behind our Financial Management team is that it has been established that local government roles and responsibilities lack clear definition which prevents them from becoming more responsive to the growing needs of their constituents.
 - When coupled with their lack of authority to establish adequate fees for public services and to adopt local tax levy rates to generate adequate revenues to meet both the growing demands for public improvements and other requirements mandated by the central level of government, local governments are challenged beyond their present day capabilities. Local governments continue to depend on the central government which has historically been inconsistent in the distribution of financial resources. As a direct result, local government budgets lack any type of meaningful purpose, let alone transparency and accountability, to serve as a management tool that clearly and concisely guides the delivery of public services and improvements.
 - The main activities within the financial management support program are;
 - Providing Technical Training for Public Finance Officials
 - Consulting on Implementing the New Budget Law
 - Improving Transparency in Finance Decision-Making
 - Increasing Accountability of Public Officials
 - Improving Budget Planning for Community Needs
 - Improving Financial Management Practices

- **Communal Enterprise**
 - The two greatest obstacles for communal enterprise performance in Serbia are a legal basis that is inappropriate for operation in a market economy and insufficient funding. Communal enterprises lack the autonomy to manage their operations effectively in a market economy. In addition, insufficient funding levels are the legacy of financial neglect that in some cases reaches as far back as 20 years. This history of inadequate funding





has left communal enterprises operating with outdated technology and obsolete equipment, and without preventive maintenance programs and spare parts.

- The main activities within the communal enterprise program are;
 - Conducting Management Training
 - Improving Operations and Maintenance
 - Increasing Public Accountability
 - Establishing Community-Based Service Standards
 - Increasing Access to Technical Developments in Operations
- **Citizen participation**
 - The underlying objective of SLGRP citizen participation initiatives is fundamental change in attitude, on the part of both municipal officials and the citizens they serve. Municipal officials should recognize the benefits of including citizens in decision-making and of ensuring that municipal government is a service-oriented operation. Citizens and NGO's should feel that municipal government is accountable to them. The citizen participation is supposed to increase citizen satisfaction with and confidence in their democratic municipal governments, as measured by changes in specific attitudes about the municipality's overall performance, openness, and inclusiveness in decision making. Achieving these objectives requires a renewed effort and more positive and cooperative attitudes among senior municipal leaders, career civil servants, civil society, and the media. What we are hoping to achieve is to get the communities to take a fresh look at the citizen-municipality relationship, establish community strategies for improvement, and begin implementing those strategies in a cooperative effort of the municipality, civil society, the media, and citizens at large. We also hope that development of citizen participation strategies will be valuable in other communities as a framework for initiating and coordinating locally-financed efforts and for seeking and coordinating outside resources.
 - The main activities within the citizen participation program are:
 - Developing and Implementing Community Strategies For Improving the Provision of Information, Citizen Participation, and Municipal Service Delivery
 - Creating Citizen Advisory Boards and Task Forces
 - Establishing Citizen Information Centres and One-Stop Permitting Centres
 - Creating Public/Private Partnerships to Revitalize Commercial Neighbourhoods
- **Information Technology**
 - The role of our Information Technology Team is somewhat different than from that of the rest of our teams. The overall goal of the IT is to provide support to most of the other teams of the Program, in addition to providing a basic core package of equipment and business software tailored to each municipality's needs to raise them to a standard minimum level of information technology utilization. Apart from the technical part of the core package, such as network cabling and equipment procurement and installation, our Information Technology Team provides the necessary education in the form of training in system administration and the use of basic software. Regular site visits, training, and hands-on technical assistance will follow any hardware or software installation to monitor the absorptive capability of municipal staff and to ensure the equipment is being effectively and properly utilized.
 - The main activities within IT support are:
 - Upgrading Data Management and Communication Systems in Local Government
 - Establishing a National Internet-based Municipal Information System





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- Providing Municipal Management Software
 - Training Municipal Staff in Basic Information Technology Applications
- **Policy reform**
 - The establishment of the Policy Reform Team was necessary because although the government of Serbia is committed to the success of independent and democratic municipal governments, there are serious problems with the major laws regulating the municipal sector.
 - The Policy Reform Team's goal, therefore, is to support the development of institutional, advocacy, and policy research environment that will facilitate the continuous improvement of Serbia's system of local democracy, including the further decentralization of public services to appropriate levels of sub-national government. The Policy Reform Team exists to improve the abilities of all relevant stakeholders to engage in informed and constructive policy analysis, formulation, and debate. Our team does this through supporting policy process related to local government authority, assisting in developing legislative monitoring system, providing technical assistance for legal reform related to decentralization, and increasing transparency in policy reform process. The Policy Reform Team also works on increasing the capacities of the anticipated Ministry of Local Government and the Ministry of Finance to formulate and implement sound policy. In addition, because the improvement of major legislation is a difficult task that requires painstaking analysis, consensus building, and deliberation, the Policy Team works aggressively to place the fundamental policy issues on the table as fast as possible, and to insure that they receive constant attention and monitoring throughout the life of the program.
 - The main activities within the policy reform program are:
 - Assisting the Policy Development Process Related to Local Government Authority
 - Providing Technical Assistance for Legal Reform Related to Decentralization
 - Providing Comparative Studies of Regional Experiences
 - Increasing Transparency in the Policy Reform Process
 - **Association development**
 - Our Association Development Team has one, single priority, and that is the Standing Conference of Towns and Municipalities. This team's objective is to stimulate and support the development of the Standing Conference of Towns and Municipalities as the local government association in Serbia. What we are hoping to achieve, is to have the Standing Conference which is able to demonstrate it is a voluntary, member-driven association representing and serving local government. It has to be emphasized that, for achievement of the results targeted by SLGRP, the Standing Conference presents a valuable tool. As the organization of local governments, the Standing Conference can become a major instrument for increasing the capacity and competence of local governments, their leaders and staff. It is our wish that the Standing Conference becomes an essential venue for training, technical assistance, policy formulation and implementation, for building coalitions and support for responsive, effective local government which fulfils the interests of citizens. Precisely because it can credibly represent local governments, gathering and assimilating their input, the Standing Conference can become a trusted and reliable conduit to and from local government and local officials. For every component of the SLGRP, the Standing Conference can

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become, indeed must serve as, a vital link in the decentralization and democratization process in Serbia. Our strategy in assistance to the Standing Conference is to serve in the role of a leveraged 'honest broker' to foster and facilitate internal dialog and focus upon internal organizational development needs.

- **The main activities within association development are:**
 - Expanding Membership Participation
 - Providing Professional Assistance in Developing Strategic Plans for Municipal Advocacy, Organizational Development and Sustainability
 - Providing Technical Assistance in Membership Development, Representation and Communications
 - Providing Training for Professional Staff Development

Project cost accounting for communal enterprises

One of the projects in the field of financial management concerns "Unit cost calculation for invoicing for communal enterprises" implemented in 2003³⁸, which focuses on water and waste water communal enterprises. The report summarizes that many communal enterprises operate at a loss, especially when cost of depreciation are not taken into account. This means companies have no savings for investment leading to further worsening of the financial situation. The project has resulted in a Manual for setting up real cost accounting methods for communal enterprises to enable to cover all costs in the near future.

Project dissemination is not known, but is assumed to be done through other activities under the USAID program.

The Ministry of Local Self Government

We have tried several times to contact the Ministry of Local Self Government regarding the Transformation of Public Enterprises, but could neither obtain more information on the policies concerned nor find a proper meeting date for staff available.

Business Association of Communal Enterprises KOMDEL

KOMDEL is a voluntary business association of public utility companies in the Republic of Serbia, based on representation of a large number of utility companies (currently < 90). KOMDEL operates based on fees paid by the members. The public enterprises perform combined activities in the field of solid waste, maintenance of green market, maintenance of public gardens and cemetery maintenance³⁹. Most of these PUC's are relatively small and have between 10 – 15 staff on their pay roll.

The main co-founder of KOMDEL is the profit organization TTI Group representing the 90 PUC's and performing as a consultant organization.

In this respect KOMDEL, as a non-profit organization, is balancing between its interests with those of TTI-Group, having a profit motive. As both are so much related to each other the outcome of this balancing act is not always very clear. At one side KOMDEL should strive towards representing all

³⁸ USAID Report by Zoltan Kristof " Manual of real unit cost calculation, billing and collection policy" for water and waste water communal enterprises, Belgrade 2003.

³⁹ Interview Mr. Lazar Krnjeta and Mrs RadmilaTrifunović, experts of KOMDEL, 9 October 2006.





PUC's in 160 municipalities in Serbia, but on the other hand it services its members in its main capacities.

KOMDEL has an Assembly and Management Board with participation of representatives of the PUC's of which 19 in the Management Board and 5 in the Assembly.

One of the main studies⁴⁰ on the options for transformation of public utility companies has been done by KOMDEL in 2004. This Study has a larger objective trying to develop a view to the benefit of all public utilities in the country. The results of the study are based on organizing discussion platforms and a series of individual discussions with directors of PUC's.

The study describes the current position of communal enterprises in terms of legal status, capital and property, financing and pricing policies. One of the main themes in the study is reflection on current laws and implications for public utility companies in Serbia. Also attention is given to developments of public enterprises in other countries such as Hungary and Romania.

Concerning the position of communal enterprises the study points out that PUC's are based on institutional monopolies with direct political control by the founders (municipalities) and direct control on tariffs, keeping prices significantly lower than market pricing as municipalities more often opt for popular policies of low pricing, preventing full cost coverage of communal services.

The revenues of most communal enterprises are generated from 3 categories of clients:

- Individual citizens or households
- Industries or companies
- Municipality or other public entities

A great problem in all public utilities is cost coverage of services. As tariffs are decided by their owners, communal enterprises are not really charged to rationalize their services.

The determination of tariffs for public utilities is one of the main instruments to balance budgets, but the position of PUC's has deteriorated in the period 1992 – 2000, initially as prices could not keep up with hyperinflation and later because municipalities preferred low pricing to keep customers satisfied. This has caused underinvestment resulting in obsolete infrastructures and technology and worsening of the efficiency in communal enterprises.

In the study some specific examples are given of tariff changes in the period 1997 - 2000:

- Solid Waste collection with actual decrease of prices of – 52,80 %
- Water and Sewerage with actual price decrease of - 51,60 %
- District heating with actual price increase of 52,40 %

It was soon realized that continuing with this “anti-monopoly regulation” would lead to greater problems, for which reason the regulations was abolished and price increase had to catch up again in these sector with average increases of between 100 % and 300 %. Only in the year 2003 for the first time in many years a real price increase was realized.

⁴⁰ Optimal models of transformation and privatization of communal enterprises in Serbia, Komdel - Belgrade 2004.





Currently the communal tariffs are restricted through Government decrees of the Ministry of Finance setting targets in relation to inflation in the country.

In the report recommended directions for changes are indicated while looking outside at developments in European countries. It is noticed that some common elements have occurred in these developments such as:

- Tendency towards increasing efficiency by means of privatization;
- Reduction of the role of the State by means of deregulation;
- Tendency towards decreasing budgetary deficits by decreasing the volumes of public consumption

For this reason different forms of increasing private sector involvement are taken into account trying to incorporate lessons learned from good and best practices in transitional countries.

The KOMDEL study refers to practices in other countries regarding the position of public utilities and the legal framework regarding communal enterprises. It provides recommendations for directions of change including consolidation of communal enterprises, and new models for PUC transformation and privatization.

The study results in a plea for a transformation strategy of public utilities from the GoS covering all areas of laws and regulations to legal status, transfer of assets and other instruments of management of public utilities in the country

As for directions of change the study recommends to take into consideration:

- Different mixed forms of ownership of public enterprises ranging from majority shareholder ship by the municipality to full transfer to private sector or use of concessions, BOT contracts, management – and service contracts.
- Change in attitudes towards public utility infrastructures, mainly leading in to more explicit requirements of services making public utilities more transparent for its stakeholders.

As a result of the study some activities are prioritized for future actions at:

1. **national level**, such as:
 - Passing and upgrading of regulations concerning status issues and independence of municipalities
 - Formulating principle interest of state in general and political harmonization with local government
 - Defining the strategy and framework for utility systems transformation at national level.
2. **local level**, such as:
 - Defining an overall utility systems transformation plan;
 - Defining the restructuring program for all existing communal enterprises
 - Determining specific solutions





As targeted areas for transformation of PUC's are indicated:

- Water supply and sewerage system
- Facilities for drinking water treatment
- Facilities for waste water treatment
- Landfills

Technical Assistance GTZ in Modernization of Municipal Services

The German Agency for Development Cooperation (GTZ) is since December 2001 involved in a technical assistance project with the objective "to strengthen the capacity of Serbian Local governments in providing basic services to their citizens."⁴¹ The project initially envisaged to last till December 2006 is expected to be renewed till December 2008.

The key partner involved in developing sustainable support structures for the advancement of local government in more efficient municipal administrations is the Standing Conference for Towns and Municipalities (SCTM), which cooperates with GTZ in various committees covering main subjects of municipal administration

GTZ indicated that the following committees within the SCTM are the most relevant for the subjects covered in this report:

- The Committee on Municipal Public Services and Housing
- The Committee on Energy Efficiency

Most of the Committees have working groups addressing main problems, most of them have recently started their work and focus on initiating pilot projects and demonstration projects in different areas of municipal services.

One of the interesting developments is the set up of a regional cooperation project of municipalities in South Eastern Europe (SEE).

After initially being supported since the year 2001 by the Council of Europe the formal inauguration of the "Network of Associations for Local Authorities in South Eastern Europe (NALAS) took place in September 2005 in Skopje. The network aims at establishing a common working structure for all of the (currently) 12 NALAS Member Associations in the Stability Pact Area. The goal is to organize a systematic exchange of information and enhance regional cooperation in order to contribute to meeting the challenges of EU association on the local level. Working platforms for regional cooperation is being established. Efforts are made for NALAS to become a "Focal Point for municipal services" for all members.

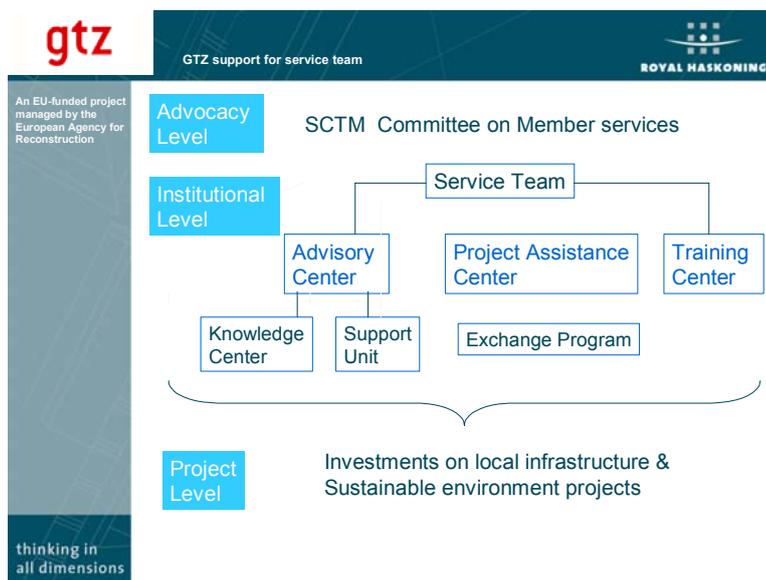
The GTZ project defines different level of operations such as the political level, institutional level and project level as indicated hereafter.

⁴¹ GTZ Brochure: Modernization of Municipal Services' from Project Office Belgrade 2006.





GTZ has drawn up an institutional structure covering activities concerning the “modernization of municipalities” as indicated below:



This institutional structure gives increasingly guidance to technical assistance efforts, but also has a growing function in “networking” among all municipalities participating in the SCTM.





Technical assistance VNG to SCTM

The Dutch Vereniging Nederlandse Gemeenten (VNG) is providing support to the SCTM in two main areas⁴²:

- Development of Business Plan
- Development of Twinning concept

Development SCTM Strategic Plan⁴³

This Strategic Plan constitutes a logical follow up of the Strategic Plan 2003 – 2004. It is a co-production of SCTM management and staff and SCTM member's representatives with the support of SLGRG and VNG International (International Cooperation Agency of the Dutch Association of Local Authorities) as facilitators.

A workshop on Strategic Planning was held in Palič from 12 – 14 November, 2004. Participants were SCTM management and staff, SLGRP staff members, representatives of SCTM members and donors.

Based on the formulated general strategy for the coming years, the participants of the Palič SP workshop have identified a set of top-3 strategic priority areas. They are listed below in their original form. Next to that the issues of financial sustainability and institutional strengthening of SCTM are identified as continuous strategic attention areas. The top-3 strategic areas are directly related to the identified top-3 weaknesses identified in SWOT analysis.

Top-3 strategic priority areas (member oriented)

1. *Advocacy*

- 1.1 Mandatory participation/consultation of SC in drafting/adopting/implementing laws
 - Defining the platform for negotiation
 - Creating a parliamentary board for local government
 - Defining (with government) areas in which local government has to be consulted, such as local governance law and related laws, etc.
- 1.2 Enhancing mechanisms for efficient advocacy

2. *Service provision to members/relations with members*

- 2.1 Creation of resource centre (database, advisory function, legal aid to members)
- 2.2 Setting up a training centre for LG representatives
- 2.3 Stimulate creation of specific interest groups out of SC membership
- 2.4 Continuous assessment of needs and further membership information collection

3. *Communication/PR*

- 3.1 Enhancement of internal communication (with the members and within the secretariat)
- 3.2 Development of external communication (with - local as well as national - media, central government, donors, public at large)
- 3.3 SCTM Image building (instrument to achieve 3.1) = visual identity

⁴² Meeting Mr. Marc Janssen, Business Unit Manager Europe of VNG International on 15 August in The Hague.

⁴³ The Strategic Plan of the Standing Conference of Towns and Municipalities 2005 – 2008 – draft November 2004





Continuous strategic attention area (organisational)

- 4. Financial sustainability/institutional strengthening of SCTM
- 4.1 Structural income generated from
 - Members
 - Government, based on specific joint projects
 - Donors
 - Sponsorships

Own activities (fee based)

- 4.2 Financial independency
- 4.3 Training of staff
- 4.4 Internal organisation (consolidating procedures, structural ways of working)
- 4.5 HRM

Other strategic areas (continuous attention area but no short term priority)

- 5. Cooperation
- 5.1 Inter-municipal co-operation (exchange of experiences, interest pooling, joint requests to central government)
- 5.2 Regional co-operation of Local Governments (SE Europe, within Euro region, cross border co-operation)
- 5.3 International co-operation (participation in international organisations valuable to local authorities, stimulate co-operation, experience sharing, joint projects, set up a new committee - for European integration)

The Strategic Plan is leading to elaboration of Strategic and Milestones in all relevant areas.

Conclusions:

As can be derived from the SCTM Strategic Plan many activities are focused on institutional strengthening of SCTM itself, while some other topics, such as mentioned under Par 5 Cooperation, are identified, but not targeted as a short term priority. It is assumed that one is conditioning the other and external cooperation can only be successful when the internal organization of the SCTM is clearly established with all participants.

Development of Twinning concept⁴⁴

LOGO (Local Government) East is a national bilateral programme for strengthening regional and local governments in Romania, Bulgaria, Turkey, Ukraine, Serbia and Montenegro through partnerships. The programme provides a mechanism for exchange of local government experiences between Netherlands municipalities, water boards, and provinces and local government structures in the target countries. It builds on the local government twinning networks that already exist between the Netherlands and the target countries, but also aims to initiate new twinning. LOGO East is financially supported by the Social Transformation Programme Central and Eastern Europe (Matra) of the Netherlands Ministry of Foreign

⁴⁴ Report Logo East Twinning Framework Serbia, Improvement of the internal management of local governments in Serbia 2006 – 2007.





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Affairs. The duration of the programme is two years. All activities therefore have to be finalised before 30 September 2007.

In the VNG recommendations the focus of attention is given to 4 main themes:

- Citizen participation in Serbia
- Ethics and Integrity in Serbia
- Service provision in local self government
- Municipal management of local self government

One of the running projects is focusing on citizen participation in the Vojvodina region⁴⁵:

“Focus Vojvodina” aims at introducing citizen participation as a tool for policy making in four municipalities in the Serbian province of Vojvodina: Bela Crkva, Bac, Subotica and Indjija. The municipalities are linked to the Dutch municipalities of Vlist, Steenwijkerland, Leidschendam-Voorburg and Zwolle.

The projects, a joint effort of the Vojvodina and Dutch municipalities, stimulate the dissemination of skills and knowledge among citizens and civil servants, and raise the public awareness about the opportunities of citizen participation. The themes of the projects are varied and range from elderly care and youth work groups to sports & recreation and municipal management.

Working visits (to the Netherlands and Vojvodina), trainings and seminars form the basis of the programme. Carrying diverse titles such as “Project Cycle Management”, “Planning Citizen Participation and Municipality”, “Building a Civil Society” and “Joint Community Activities”, all activities have the same focus: to increase the level of citizen participation in local policy making.

All programme activities are financially supported by the Netherlands Ministry of Foreign Affairs and implemented with specialised support from the Serbian Citizens Pact for South Eastern Europe (CP), the Dutch Interchurch Peace Council (IKV) and the Polish Foundation in Support of Local Democracy (FSLD).

Currently VNG is involved in setting up twinning projects.

In the VNG recommendations suggestions are made for topics/projects of development in the area of performance indicators for Human Resource Management.

⁴⁵ Focus Vojvodina”, please see web site : www.focusvojvodina.org





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Performance indicators for improvement of human resource capacity

- job descriptions for each position (in a certain policy field);
- job appraisal system;
- classification system for the positions in the organisation according to the ISO;
- recruitment procedures;
- procedures for selection of employees
- training in interview techniques;
- handbook describing internal regulations (holiday, sick leave etc...);
- broadly supported remuneration policy;
- training plan for its employees (in a certain policy field);
- establishment of an HRM office;
- processes to disperse knowledge across the internal organisation;
- strategic plans approved by the municipal council;
- integral plan to have departments communicating;
- processes describing the functioning of the departments;
- plans to start Public Private Partnerships;
- establishment of a local Ombudsman.





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ANNEX VII

Case studies of projects in relevant sectors

11-01-2007



Municipal Infrastructure Agency Support Programme
An EU-funded project managed by the European Agency for Reconstruction
9R5927/CvS/P2006_97/R001

Transformation of Public Utility Companies in the Republic of Serbia
Report



Case study Indija	Water supply and distribution
<p>Objectives The project in Indija is aiming at development of a new water supply and distribution network. With construction of 4 new water wells in Indija, Maradik, Beska and Novi Karlovci, construction of a water distribution system in villages Ljukovo and Jarkovci, transmission to Beska-Cortanovci, improvements of water supply and quality are realised for 11 communities within the municipality of Indija, comprising over 61.000 inhabitants and over 8.000 households. The regional water system will also include the municipality of Stara Pazova comprising 10 communities with over 70.000 inhabitants and over 21.000 households.</p> <p>Funding:</p> <ul style="list-style-type: none"> • EAR grant € 1.800.00 • Commercial bank loan € 1.000.000 • Municipal contribution € 1.200.000 <p>Management and organization; The facilities and new constructions are located within the municipality Indija and will in the future be part of a regionalized water supply and distribution network. This also implies that for the moment one PUC (Indija) is involved. The PUC for Stara Pazova will be involved in a later stage and no elaboration is yet given on future structures</p>	

Case study Kruševac			District Heating
July 3 - Monday	Visit to Kruševac Municipality and PUC for District Heating	Mr. Dragan Azdejkovic, Mayor of Kruševac. Mr. Miroљjub Eric, General Manager Gradska Toplana	Discuss transformation issues PUC's at local level Relations with SCTM
<p>Objectives The project is aiming at reconstruction and Extension of the District Heating System comprising coal fired unit repairs; Oil fired unit replacement by dual fuel unit, Rasadnik; Dual fuel package unit replacement, Prnjavor; New district heating unit; Heating stations; District heating network extension by 1910 connections.</p> <p>Funding:</p> <ul style="list-style-type: none"> • EAR grant € 1.194.560 • Commercial bank loan € 1,698,671 • Municipal contribution € 424,668 <p>Management and organization; The facilities and new constructions are located within the municipality Kruševac, but have a district/regional function. This also implies that for the moment only one PUC (Kruševac) is involved. In discussion with Mayor and PUC management current problems were discussed. Gradual increase of tariffs is pursued including retrieve of invoices for unaccounted water.</p> <p>Corporatisation was seen as an option for the future as first conditions has to be put in place to guarantee a proper transformation process which secures interest of all stakeholders. One of these instruments is proper valuation of assets. Within current political environment it was believed that some groups will take advantage of privatization process to the disadvantage of users and citizens.</p> <p>Improvement of management and organization is mainly realized within current legal framework and options for improvement of PUC's. Institutional strengthening in the grant contract is covered in a general sense. Financial sustainability is covered through the net cash flows of the local public utility Gradska Toplana based on the assumption that no tariff increases will be necessary to generate appositive cash flow over the life time of the project (with exception of the 20th year when replacement investments will have to be done). Covering future investments in the tariffs is still a challenge to be decided in the near future.</p>			





Case study Žitorađa	Water supply and distribution
<p>Objectives The project is aiming at Water Supply and Construction of water supply pipelines in 5 communities</p> <p>Funding:</p> <ul style="list-style-type: none">• EAR grant € 403.963• Commercial bank loan € 134.146 (yet unknown)• Municipal contribution € 131.320• Governmental contribution: € 237.804 <p>Management and organization; As all communities are within one municipality no cooperation with other municipalities is part of the project and solutions are found within current PUC laws and regulations.</p> <p>Institutional strengthening in the grant contract is covered in a general sense. Financial viability is supported by the fact that the improvements will increase revenues from connected customers and reduce cost of water supply due to leakages of the existing pipelines and savings on health care expenses due to low quality of current drinking water.</p>	

Case study Žitište	Road development
<p>Objectives The project is aiming at Municipal Roads with a reconstruction of 6 km of local roads.</p> <p>Funding:</p> <ul style="list-style-type: none">• EAR grant € 171.324• Commercial bank loan € 168.000 (Komercijalna Banka)• Municipal contribution € 83.671• Governmental contribution: none <p>Management and organization; As all communities are within one municipality no cooperation with other municipalities is part of the project and solutions are found within current PUC laws and regulations.</p> <p>Institutional strengthening in the grant contract is covered in a general sense. Road development is a primary activity under responsibility of the municipality.</p>	

Case study Zemun	Water supply and distribution
<p>Objectives The project is aiming at Water Supply Construction of 8 km of local water distribution network</p> <p>Funding:</p> <ul style="list-style-type: none">• EAR grant € 146.369• Commercial bank loan € 210.397 (yet unknown)• Municipal contribution € 19.000• Governmental contribution: none <p>Management and organization; As all communities are within one municipality no cooperation with other municipalities is part of the project and solutions are found within current PUC laws and regulations.</p> <p>Institutional strengthening in the grant contract is covered in a general sense.</p>	





Case study Mionica	Water supply and distribution
Objectives The project aims at improvement of the water supply system with reconstruction of the main pipeline from the Razbojiste reservoir; Construction of the Dučić reservoir; Construction of a main supply pipeline for the Dučić reservoir, Construction of a distribution pipeline for the Dučić settlement.	
Funding: <ul style="list-style-type: none">• EAR grant € 154.242• Commercial bank loan € 160.284 (yet unknown)• Municipal contribution € 15.300• Governmental contribution: none	
Management and organization: As all communities are within one municipality no cooperation with other municipalities is part of the project and solutions are found within current PUC laws and regulations.	
Institutional strengthening is covered in a general sense. No other specific arrangements are mentioned other than an effort to improve collection rates from 50 % to 80 % due to network improvements.	

Case study Varvarin	Water supply and distribution
Objectives The project aims at improvement of Water Supply with the following works: a new ground water well; upgrading of water treatment plant (WTP); construction of water tower; construction of a pipeline to the water tower; rehabilitation of water distribution network in Varvarin Town; distribution network for Selo Varvarin, Donji Katun, Gornji Katun and Obrež; distribution network and water supply pipeline Donji Katun.	
Funding: <ul style="list-style-type: none">• EAR grant € 613,110• Commercial bank loan € 515,732• Municipal contribution € 688,328• Governmental contribution: none	
Management and organization; As all communities are within one municipality no cooperation with other municipalities is part of the project and solutions are found within current PUC laws and regulations.	
Institutional strengthening is covered in a general sense, while also integrated in the financial ratios mainly targeting increasing revenues, such as: <ul style="list-style-type: none">• Increase of water and sewerage tariffs with 25 % in 2007 and 25 % in 2008• Reduction of unaccounted water from 69 % to 40 % due to improvements of improvements in the drinking water network	

Case study Smederevo	Water supply and sewerage
Objectives The project aims at Water Supply, Wastewater, Reconstruction of Infrastructure with <ul style="list-style-type: none">• Rehabilitate three local streets, including the underlying infrastructure;• Extend the water distribution network to the Šumadijska villages.	
Funding: <ul style="list-style-type: none">• EAR grant € 1,706,262• Commercial bank loan € 1,954,810 (Raiffaisen Bank)• Municipal contribution € 274,001• Governmental contribution: none	





Management and organization;

As all communities are within one municipality no cooperation with other municipalities is part of the project and solutions are found within current PUC laws and regulations.

Institutional strengthening is not covered in the same way and the same structure of criteria for the other projects as the main purpose of the project is to restore primary infrastructure of municipal roads also contributing to underlying infrastructure for water pipelines and sewerage lines.

Improvement of the roads will also contribute to improvement of underground electric and telephone lines and placement of gas installations for distribution to more than 1500 apartments and 800 individual houses.

Case study Apatin	Water supply and sewerage
<p>Objectives The project aims at construction of a water treatment plant and sewerage disposal network, comprising:</p> <ul style="list-style-type: none"> • Upgrading of Water Treatment Plant • Replacement of approximately 6.7 km out of the total existing 38 km of AC water pipes <p>Funding:</p> <ul style="list-style-type: none"> • EAR grant € 375,290 • Commercial bank loan € 1,161,275 (yet unknown) • Municipal contribution € 209,029 • Governmental contribution: none <p>Management and organization; As all communities are within one municipality no cooperation with other municipalities is part of the project and solutions are found within current PUC laws and regulations.</p>	

Case study Regional Sanitary Landfill Area „Duboko“ in Cacak – Uzice	Solid Waste
<p>Objectives The cities of Cacak and Uzice, which are by far the biggest municipalities to be involved in the Regional Solid Waste Management scheme, are located in the central part of the Republic of Serbia. The region is one of the developed industrial areas in Serbia</p> <ul style="list-style-type: none"> • Nine municipalities with around 360.000 inhabitants altogether • 8 transfer stations • Transport system for transferring waste from the transfer stations to the landfill • Facilities for waste selection and classification <p>Sanitary landfill for disposal of communal waste – with lifetime estimated to be 20 yearsThe project aimsat construction of a Regional Communal Waste Management Project with:</p> <ul style="list-style-type: none"> • Construction of new regional sanitary landfill with access road and all ancillary buildings and facilities in Duboko (Uzice municipality) for solid waste disposal of municipalities Uzice, Cacak, Pozega, Lucani, Cajetina, Ivanjica, Arilje, Bajina Basta, Kosjeric • Set up of a plant for selection and classification of the communal waste in Duboko Closure, conservation and recultivation of the existing waste dump in Smederevo • Establishment of a number of waste transfer station in the abovementioned municipalities <p>Funding: Still to be determined with allocation for a total € 12.000.000</p> <p>Management and organization; The new PUC to be established willcover services for 9 municipalities and in the managerial structure lessons</p>	





are taken from another cooperation in the same region concerning water supply and distribution.
(See Case study Rzav hereafter)

This project aims at establishment of a regional landfill with 9 participating communities
With this purpose an agreement was made of founding, building and using the Regional Sanitary Landfill Area
„Duboko“ With all signatories: Municipalities of: Užice, Bajina Bašta, Čačak, Požega, Arilje, Čajetina, Kosjerić,
Lučani and Ivanjica

Inter Municipal Funding:

For the funding an allocation scheme was agreed upon reflecting the number of inhabitants of the participating municipalities as shown hereafter.

Municipality	Euro	%	Inhabitants	%
Užice	1.428.811,00	23,91	83.022	22,38
Bajina Bašta	501.369,00	8,39	29.151	7,86
Požega	555.748,00	9,30	32.293	8,70
Arilje	340.620,00	5,70	19.784	5,33
Čajetina	268.910,00	4,50	15.628	4,21
Kosjerić	240.824,00	4,03	14.001	3,77
Lučani	423.683,00	7,09	24.614	6,63
Ivanjica	609.530,00	10,20	35.445	9,55
Čačak	1.606.292,00	26,88	117.072	31,55
Total	5.975.787,00	100,00	371.010	100,00

This was confirmed in Clause 5

The parties to the agreement made decisions concerning amounts of money and percentage, regarding to the previous Clause of this agreement and according to the total number of citizens of every municipality signatory (according to the official census from 2002).

As can be seen from the table the percentage of inhabitants does not exactly reflect the funding allocation and some adaptation was made for (unknown) reasons of interest for the participating communities. For Užice the slightly relatively higher funding percentage may have to relate to the fact that the landfill is established in this municipality.

PUC „Duboko“ – Užice

For the purpose of the project one new regional PUC was established.

Company's name: Public Utility Company „Regional Sanitary Landfill Area Duboko“ – Užice

No reference is made to what will be done with current PUC's in the solid waste area of the participating municipalities.

The Company is directed by the **Governing Board**, consisted of one representative of each party.

The Company's Governing Board is obliged to in a period of one year from the day of signing the agreement to complete the procedure and to elect the **Company's Manager**.

Allocation of profits:

Company's profit concerning sale of secondary raw material, bio-gas and compost, is in the property of the Company and is used for technological improvement of the system for handling the Landfill Area. Part of the Company's profit can be also used for unpredicted utility investments of municipalities signatories, as a result of the way of functioning of the regional system for handling the Landfill Area.

The decision of distributing financial means from previous States of this Clause is made by the Company's **Governing Board**.





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Parties are agreed that the Company's Governing Board establishes by its own decision:

- road direction for transporting garbage from the parties' territories
- the price of dumping garbage on the Landfill Area, paid by the parties

Assessment after one year in operation:

In order to determinate the exact quantity of waste which is the reason for changing the starting percentage of the participation in financing the Landfill Area, after one year from the exploitation of the Landfill Area, the parties agree to measure the quantity of waste in a one year's period and, if needed, to change Clause 4 of the agreement by the Appendix. This Clause 14 suggests that the municipalities may consider future management and investments based on use of the landfill in terms of waste delivered and not related to the number of inhabitants of the municipalities.





Case study regional water supply system Rzav:

Water supply and distribution

Objectives

The PUC for water supply Rzav was funded by the municipalities of Arilje, Pozega, Lucani, Cacak and Gornji Milanovac in 1990.

Funding:

The founders realize their rights in proportion to the capital invested in the PUC, which was at the time provided from the state and municipalities budget.

Management and organization;

The bodies of the company are the following:

- **Management Board** of 11 members, 1 from each of the municipalities-founders while five are appointed from the municipality of Cacak; one representative of the employees and one representative of the Ministry of agriculture, forestry and water management.
- **Supervisory Board** consisting of five members, consisting of one representative from all municipalities-founders
- **General Manager** selected by agreement of all municipal parliaments

Special body of the PUC Rzav is the **Coordination body** consisting of the founders representatives. The Coordination body was established to assure unity in further construction and use of the system Rzav

Statutory acts of the PUC Rzav

- Agreement on construction and use of the water supply system Rzav dating from 1987 and 1990
- Decision on funding the PUC, dating from 1987 and 1990
- Articles of Association tailor-made for new PUC Rzav
- Contract on delivery of water concluded between the PUC Rzav and the 5 municipal water supply PUCs, that specifies quantity and quality of water, location of delivery and water metering, water tariff and conditions of payment, events in which quantity of water may be reduced or undelivered
- Contract on joint investment and financing of the water supply system (renewed every year)
- Contract on joint investment with the Ministry of agriculture, forestry and water management (renewed every year)

Collection rate (payment of PUCs to PUC Rzav) is in range of 50% to 91%. Measures taken to improve payments to the PUC Rzav: all PUCs were asked to submit blank drafts(bills) as a guarantee for regular payments. Two PUCs submitted blank drafts(bills) and these were activated. PUC Rzav also decreased quantity of water delivered to one of the PUCs until the blank bill was submitted.

From discussion with PUC manager Mr Lazovic:

1. All decisions on functioning of regional system must be ratified by each of the municipalities-founders. In statutory acts of Rzav it is specified that the decisions must be made within 3 months. There is no legal instrument to avoid parliamentary decisions.
2. Rzav proposed that official decision on water supply in each of the municipalities would be changed and include also Rzav system along with obligations on payment and guarantees (either cheque of municipal budget) Such Decisions also have to be adopted by the parliament.
3. Corporization was discussed at the very beginning (Republican Electricity Company was taken as an example) yet municipalities were reluctant to accept it, because of losing influence.
4. Decision making in Rzav MB is made by simple majority (51%) where the representative of employees/syndicate also have voting/decision making rights.





Case study Pirot		Solid Waste management	
October 5 Thursday	Office Royal Haskoning	Mayor Pirot Mr. Vladan Vasić	Institutional arrangement in proposed project on solid waste in Pirot and 3 neighbouring municipalities
Objectives This project was developed in the framework of Technical Assistance to the Municipal Support Programme Eastern Serbia with support of the GTZ Municipal Development Consortium. The project is aiming at: <ul style="list-style-type: none">• Construction of regional sanitary landfill in Pirot for communal waste disposal of Pirot and neighbouring municipalities – Babusnica, Dimitrovgrad, Bela Palanka			
Funding: Still to be determined in construction phase with Feasibility Study currently under development and approval			
Management and organization; <ul style="list-style-type: none">• The public utility will be a regional public utility, while the participating municipalities will maintain their existing PUC's. The reason is that the PUC's of the participating municipalities are also performing other functions than solid waste removal.• The Mayor confirms arguments for the need for such Cooperation Agreements as in the past decision making could be blocked by one of the participating municipalities and frequently has done so in real practice. Issues would be topics such as appointment of a new Manager or other issues which may have specific interest for an individual municipality.• Although the regional landfill may be in the longer term a merger of activities of all participating municipalities, in general the local municipalities and/or PUC's have a strong tendency to maintain control over the PUC's of that municipality and all powers connected to that.• The Committee for Coordination of activities consist of 2 representatives of each municipality and functions as a common Management Board for the new public utility. Pirot will finance half of the needed funding from the municipalities while the 3 others will take care for the other 50 % contribution together.• The Executive Management of the new public utility will take over all powers of the Committee for Coordination upon establishment and start of the company in a later phase.• A Cooperation Agreement was made for all municipalities involved in which all 4 municipalities will have two representatives on the Committee for Coordination in spite of the fact that Pirot represents 2/3 of the total number of inhabitants of all participating communities in the region. As the regional landfill will be on the territory of Pirot this municipality will have a major stake, but equal voting rights of parties in the construction phase contributes to decision making.• Many aspects of cooperation still have to be worked out in the elaboration of the Plan based on the Feasibility Study.			





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ANNEX VIII

Comparisons of developments in restructuring of the water sector in former EU Accession countries⁴⁶

⁴⁶ Comparative Review of Water Sector Restructuring in the EU Accession States, Work Package 1, Final Report
EU FP5 "Intermediaries" Project September 2003

11-01-2007



Municipal Infrastructure Agency Support Programme
An EU-funded project managed by the European Agency for Reconstruction
9R5927/CvS/P2006_97/R001



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This report focuses on the status of water sector restructuring across the EU Accession states. It is the outcome of the first work package, undertaken between November 2002 and September 2003 of a wider EU Framework 5 project.

Hereafter some examples are taken of some countries of relevance to Serbia supplemented with a short comparable notice on the current situation in Serbia.





Bulgaria
<p>Liberalisation</p> <p>A process of decentralisation of responsibility for the water sector from the central state to municipalities began in 1991. New legislation in 1999 consolidated the potential for state ownership, municipal ownership (which could be part private) and fully private ownership. Responsibility and ownership of water/wastewater utilities has been almost fully transferred from the central state to municipalities, including management of water supply and sewage treatment, regulating prices, services and investment. In 2001 the government suspended further private sector involvement.</p>
<p>Commercialisation</p> <p>Municipalities have commercialised water management including: clearer definitions of water users, specification of contracts for maintenance, metering of clean water and sewage, specification of how water and sewage is paid for, the conditions in which water supply and sewage collection are terminated, and the introduction of water prices.</p>
<p>Private Sector Involvement</p> <p>There have been two forms of private sector involvement. First, 'Water Associations', of which there are 4, although 3 are contracted to one municipality, are private companies formed by employees and consumers. Departments transfer their managerial functions to the Water Associations, including transfer of 'the right to use' water/wastewater utilities for a period of 10 years. Water associations are responsible for managing, investment, day-to-day maintenance, metering and pricing, communicating with customers. Water and Sewage Departments retain the ownership and control on investment priorities. The second form is the concession of which there is only one, in Sofia given to an "ad hoc" private sector company jointly owned by a British-American consortium and the Municipality of Sofia for the operation and maintenance of water/wastewater for 35 years.</p>
<p>Country specific issues</p> <p>Key problems of water loss and establishing responsibility for metering, control and reducing such loss.</p>
<p>Future Trajectories</p> <p>Further private sector involvement of assets has been planned in two city areas, however, these have been postponed due to concerns of transparency and corruption experienced with private sector involvement in Sofia. The government has suspended private sector involvement, however, new legislation is expected to consolidate the legal context for private concessions and water associations.</p>





Czech Republic

Liberalisation

The current legislative framework has liberalised the water sector primarily by permitting the private sector involvement of water companies. The liberalisation of the water sector is founded on the Large Privatisation Act (1991), which foresees the transfer of rights and the sale of shares to private companies; the Amendment to Small Businesses Act (1996), by which rights over water supply and sewerage systems became licensable and were transferred to private companies; and the "Act on Water Supply Systems and Sewage and Drainage Systems" that defines the standards for concessions of operators for drinking water supply and wastewater disposal. The private sector involvement of the water sector was implemented during the second stage of coupon privatisation (1993-1995).

Commercialisation

Drinking water supply and waste water sewerage is managed in most cases by private companies. Prices are fixed by the municipalities according to the restrictions of the Ministry of Agriculture and the Ministry of Environment. Nevertheless there have been dramatic increases in water prices.

Private sector involvement

The water sector is almost fully privatised, as the ownership of water/ wastewater companies has been transferred to private investors. Private companies act as operators while the ownership of the water infrastructure remains in municipal hands. Water management companies like the river basin boards are in public ownership.

Country specific issues

The fragmentation of the water sector, which poses an obstacle to efficient water investment and the dominance of large multinational companies (Vivendi, Ondeo, Anglian Water).

Future Trajectories

All experts see a trend towards more private involvement. The Czech trade union CMKOS expects that in the future two multinationals (Vivendi and Ondeo) will control up to 90% of the Czech water market. There is also still need for a regulatory body for the water sector and a fixed definition of 'water' and water rights in the Czech constitution. Finally, to meet the challenges of limited public finances and the need for investments considerable effort is needed to educate staff in water management issues.





Estonia
<p><i>Liberalisation</i> The water sector is liberalised in respect of the extraction of water resources and provision of services through the Competition Act. However the ownership of groundwater according to the Water Act (1994,1996) vests in the State.</p>
<p><i>Commercialisation</i> Environmental investments programs and especially the Small Municipalities Environmental Program (SMEP) and Small Municipalities Investment Programme (SMIP) has facilitated new management practices in over 30 municipalities. The limitations of commercialisation are currently the lack of competent personnel and finance for investment.</p>
<p><i>Private Sector Involvement</i> In the early 1990s the water sector was owned by the state but the ownership was transferred to municipal enterprises after a decision to privatise all state owned enterprises. The municipal enterprises are now public limited companies. There is one case of municipalities delegating ownership and responsibilities to a private company in the capital Tallin. In 2001 the city of Tallin sold 50.4% of the shares to the private company International Water/United Utilities.</p>
<p><i>Country specific issues</i> Since 1996 major investments have been made in sewage treatment and environmental protection through national and international investment programs based on non-private sources. Estonia nearly complies with the EU Water Framework Directive.</p>
<p><i>Future Trajectories</i> The future trajectory seems to be commercialisation as a part of modernising the municipal water utilities and creating a stable economy. While it is legally possible to develop further private sector involvement, it is an open question if the first experiences from Tallinn will be followed in other areas.</p>





Hungary

Liberalisation

As a part of a wider decentralisation process in the early 1990s, ownership of water utilities was transferred to municipalities, including responsibilities for defining water and sewage fees. This also enables the municipalities to introduced privatization.

Commercialisation

Municipalities had to transform water and sewage works into a commercial company by the end of 1996. Legislation states that revenue from fees must cover the justified expenses though there is no central price setting formula. For water companies with high expenses there are subsidies from the Ministry for Environment and Water. Emphasis has been placed on rationalisation of operations in order to avoid producing losses, though this has been limited to large companies who had the appropriate expertise and knowledge. In the case of smaller companies, lack of competent experts and political dynamics have limited the uptake of commercialization.

Private Sector Involvement

Water companies were privatized in six large cities and in one smaller region. The privatized sector covers about 20-25% of the water supply of the Hungarian population. Foreign investors established concession contracts for 15-25 years the municipality retaining the majority ownership in water companies. But the management boards tend to be dominated by the representatives of the foreign companies.

Country specific issues

There is no central policy for water privatization, the municipalities themselves have to decide on the mode of operating the water companies. The revenue from privatization was not spent on sector improvement, however, significant developments are needed to meet EU requirements. In the case of some privatized water companies, problems emerged that raised the question of transparency of the privatization process and the capability of the municipalities in negotiating contracts.

Future Trajectories

There is likely to be mergers between smaller water companies to generate economies of scale. EU requirements place pressure on more professional and efficient operation and this could lead in some cases to further private sector involvement. There is increased interest from domestic investors in the water sector.





Latvia
<p>Liberalisation Under the Law on Environmental Protection (1991) local government are responsible for the utilisation of natural resources within their own administrative territory. The Law on Water Management (2002) states the right to use water and water bodies for personal and commercial purposes in accordance with this law and other legislation. Law on Regulators of Public Utilities (2000) states that water supply and sewerage should be regulated by local regulators</p>
<p>Commercialisation The water sector has been decentralised, with ownership moving from the state to municipalities. Water services are normally provided by special purpose companies owned by the municipalities. The utilities are, in principle, dependent on tariff revenues and legislation allows for profit generation from tariffs. In practice tariffs hardly cover the costs of operation and certainly not the investments necessary for the water sector to meet the demands of the EU water frame directive. Foreign support for technological and managerial development has been important.</p>
<p>Private Sector Involvement Different kinds of private ownership of water utilities can be identified, for example private water supplies in rural areas, wastewater treatment within industry, and private sources of financing for individual connections to the centralised systems (including the installation of meters). There are no examples of transferring either the ownership of public water utilities or the concession of services to private companies.</p>
<p>Country specific issues Latvia is close to complying with the EU technical standards of water supply and wastewater treatment. The great challenge to the water sector is the implementation of River Basin Management. As many municipalities are very small in terms of population they do not have the capacity to manage and develop the water sector. Regional reform seems necessary but politically difficult to achieve.</p>
<p>Future Trajectories The government at the moment states (by law, contract or agreement???) that the water sector will not be privatised, but legislation has been prepared for private sector involvement and a plan from the Ministry of Environmental Protection and Regional Development points to private sector involvement of municipal water utilities in 5-10 years. Indeed, large companies have shown interest in the water utilities of the two largest cities.</p>





Poland
<p>Liberalisation Restructuring in the early 1990s transferred responsibility and ownership of water and wastewater utilities from the central state to the municipalities. The Law on Local Government (1990) created the utilities as municipal budgetary units. The Law on Municipal Management (December 1996) required the transformation of the utilities into commercial law companies.</p>
<p>Commercialisation Utilities exist as commercial law companies and, contrary to the requirements of the 1996 law, as budgetary units, water associations or State owned companies. Municipalities are now responsible for the management of water supply and sewage treatment, regulating prices, regulating services and investment.</p>
<p>Private Sector Involvement The majority of utilities are owned by the municipalities, with the exception of a few cases where private investors are also involved. In the case of Gdansk, where the need to improve the water and wastewater infrastructure was very urgent, 30 years lasting contracts between the local authorities and a private investor were concluded in the early 90s.</p>
<p>Country specific issues The Polish water and wastewater sector was in a very poor condition due to the neglect of its development by the former socialist government. In the 1990s the priority was providing for the needs of industry rather than improving the level of service provided to citizens or protecting the environment. Given the high and growing unemployment rate in Poland and the financially difficult situation in some regions, municipalities are not always able to provide their part of the investment and therefore need the financial backing of private investors.</p>
<p>Future Trajectories Polish municipalities are particularly keen to acquire ISPA (Instrument for Structural Policies for Pre-Accession) grants that allow towns and cities of more than 100,000 inhabitants to apply for funds to improve their water and wastewater infrastructure in order to meet EU requirements. To access these grants the municipalities need to contribute around 35% of the total required investment themselves. Some of that 35% is likely to be raised from private investors.</p>





Romania
<p>Liberalisation The Law on Water (1996) and the Law on Environmental Protection (1995) set up the legislative framework for environmental, economical, quality and consumer regulation (that are in accordance with the EU standards) and allowed for private sector involvement. Decentralization included the transfer of ownership of water and waste water utilities to municipalities. Municipalities can choose the mode of service operation, as municipal enterprises, commercial companies, or public services (within the executive structure of the municipalities, as concession or leasing contracts). Water tariffs are defined centrally. Surveillance of the sector is undertaken by the Ministry of Water, Forestry and Environmental Protection and the National Company of Romanian water (established in 1999).</p>
<p>Commercialisation Signs of commercialisation are present as municipalities have separated different functions into specific organisations in order to establish better transparency and efficiency. These processes are more developed in the larger cities.</p>
<p>Private Sector Involvement Ownership of the utilities is retained by municipalities and the management and responsibility for development of the public assets was commissioned to foreign investors. Private sector involvement is a high priority in government strategy to raise revenue for reconstruction and development. Four water companies (Bucharest, Ploiesti, Falticeni, Timisoara) have been privatised so far in the form of concession contract for 25-49 years. Further three water companies are under private sector involvement process.</p>
<p>Country specific issues There is a significant lack of provision of water and sewage infrastructure in rural areas. There is also no clear distribution of competencies between the municipalities and overlaps and conflicts occur between the two tiers of local and regional level. The regional municipalities deal with the regional water supply system and coordinate the investments made by rural local councils. The local municipalities' legislation and mechanisms are often not prepared for transparent and sufficient private sector involvement.</p>
<p>Future Trajectories There will be more commercialisation in the sector as it is seen desirable to foster the profitability and economic efficiency of public services. More municipal enterprises will be turned to commercial companies and the intention is to integrate the small public service providers. The private sector involvement of public services is regarded as high priority in the Government strategy in relation attracting investment and as a means to meet the consumers' requirements.</p>





Slovakia

Liberalisation

The water sector has not been liberalised and is slowly being reformed, with the objective of devolving control from the state to the municipal authorities. 'The Conception of the Transformation of the State Water Works' (July 2002) clarified this process which was first initiated in 1997. It was agreed that the five state-owned regional water and sewerage bodies would be replaced by seven regional joint-stock companies that would then transfer ownership of the water infrastructure to municipalities or associations of municipalities upon their request.

Commercialisation

Apart from the transfer of ownership of the water infrastructure to municipalities there is little evidence of commercialisation at present, though this is likely to change dramatically as private sector involvement increases.

Private Sector Involvement

Once municipalities have taken ownership of the utilities (by the end of 2003), they are free to involve the private sector through selling part of their company to an investor or signing a long-term leasing/operations contract with a foreign operator. As of 2002, three municipal associations had taken control of their water and sewerage utilities. This accounts for 5-6% of the population. Only Trencin has 'delegated' control of its utility to a private foreign company, Suez Lyonnaise des Eaux.

Country specific issues

Once these transfers are completed it is expected – and hoped by the Government - that many municipalities will follow the path to assist them in undertaking the major improvements required to update the decaying infrastructure, improve environmental standards to bring the country in line with the EU and make the utilities more cost effective in general through the introduction of private sector practices and foreign management expertise.

Future Trajectories

The debate over the merits of private sector involvement is far from over - indicated by resistance to private sector involvement in Komarno and Hlohovec. Many foreign water companies are interested in market investment. Some municipalities in largely rural areas have not taken over ownership and control of the water and waste-water sector and it is unclear what will happen.





Slovenia

Liberalisation

Water/wastewater sector legislation is based on the Water Act (1999, 2001) and the National Programme of Water Management (2002) introducing economic valuations of the use of water, payments for water rights (acquired on the basis of a water permit or concession), and includes compliance with the EU directive on Common EU Waters. Regulation is undertaken by the state in the area of water regulation, maintenance of the existing infrastructure and investment in protection against the harmful effects of water.

Commercialisation

Up until 2001 none of municipality water companies had been restructured. It is planned that the bulk of tasks now carried out by state will be handed over to the regions. Municipalities will carry out all tasks on their level on the principle of proportionality (financial resources in proportion to the tasks) and the principle of self-financing (revenue raising from own taxes, etc.).

Private Sector Involvement

There is one form of private sector involvement - concession. One water utility is privatised. The concession is given to a multinational consortium who have majority ownership of the company given the concession for 22 years.

Country specific issues

Due to the increasingly restrictive monetary and fiscal policy in Slovenia, the economic policy of water sector – and in particular, the application of economic instruments for implementing it – is a priority. To ‘cover’ the gap between the required and provided funds, emphasis is placed on improving the efficiency and effectiveness of operations and more sustainable use of water.

Future Trajectories

The proposed constitutional amendments enforce the principle of subsidiarity and encourage the process of decentralisation. A new policy is being developed that will set up legal and economic mechanisms for: establishing an economic price for the use of water; establishing sustainable management of the natural water resources; promoting a sustainable system of waste management and reducing quantities of waste at source. Between 5% and 52% of the equity in the water companies is planned to be sold to key investors (starting 2001). Concessions will be introduced for the right to use water (starting 2002).





Serbia

Liberalisation

Presently assets are owned by the Central Government (the Republic) while the municipalities are responsible for arranging and managing communal services including water supply and waste water. The new Constitution of November 2006 opens possibility for transfer of ownership to the municipalities. Tariffs are set at municipal level and there is considerable difference in between the municipalities, not only in level of tariffs, but also coverage and unaccounted water. As of January 2006, the Central Government sets the limit on overall tariff increase at 9,3 % at annual level. Overall responsibility for the water and waste water sector belongs to the Ministry of Agriculture, Forestry and Water Management and their Directorate for Water. The Main legal document is the Law on Water (1996).

Commercialization

There is no evidence of commercialization. The tariffs are at the best set at the level of covering cost of operations and maintenance. Utilities operate as Public Utility Companies under the Law on Public Companies and Performing Activities of Common Interest, and for major decisions approvals of municipal assemblies are required.

Private sector involvement

There is a legal possibility for the Municipalities to entrust communal services to a private operator. However, until now there has not been private sector involvement in water or waste water sector.

Country specific issues

The period of 1990s until 2004 was characterized by no investment due to which equipment is in dilapidated state and there is high need for investment in the sector. The state does not have sufficient funds to invest in sector.

Future Trajectories

The new Constitution envisages that Municipalities would have their own property. A set of legislation is required to enable application of the possibility. There are initiatives to promulgate new Law on Waters which would include tariff setting, specify educational level of water companies' managers and create integrative approach to water management. The Government announced a possibility of preparing a strategy for transformation of communal services.





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ANNEX IX

Benchmarking water sector performance in Republic of Serbia

11-01-2007



Municipal Infrastructure Agency Support Programme
An EU-funded project managed by the European Agency for Reconstruction
9R5927/CvS/P2006_97/R001

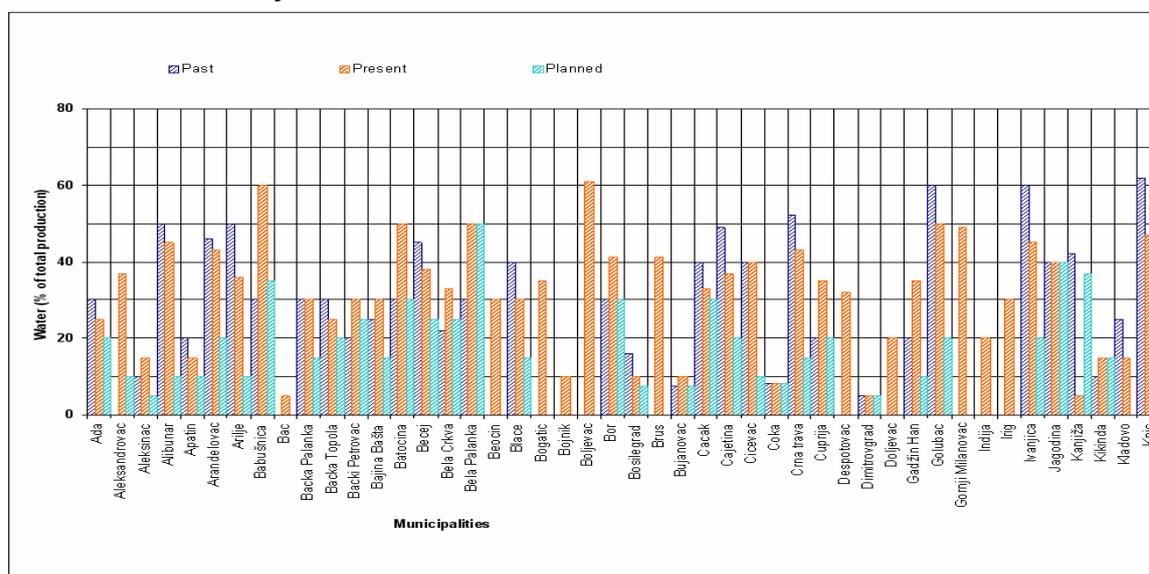
Transformation of Public Utility Companies in the Republic of Serbia
Report



Water losses

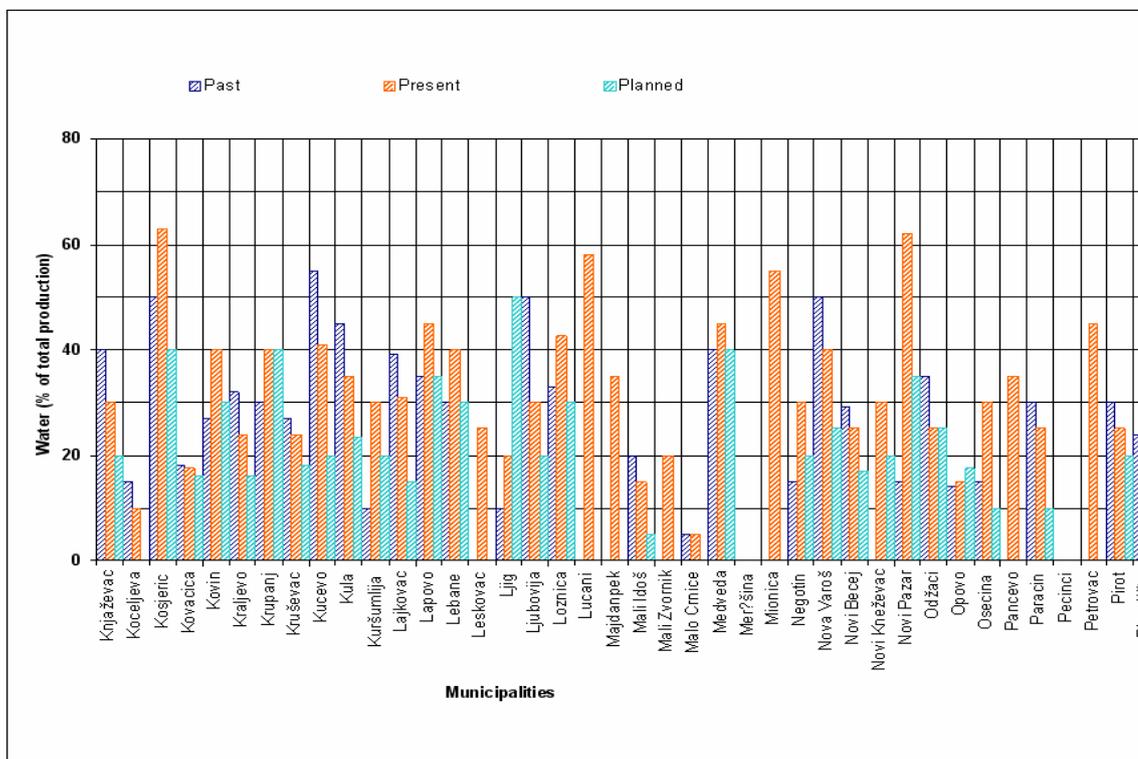
One of the benchmarking criteria focuses on **water losses** ranging from 5 – 65 % in the municipalities in Serbia.

Water losses in the system





Water losses in the system

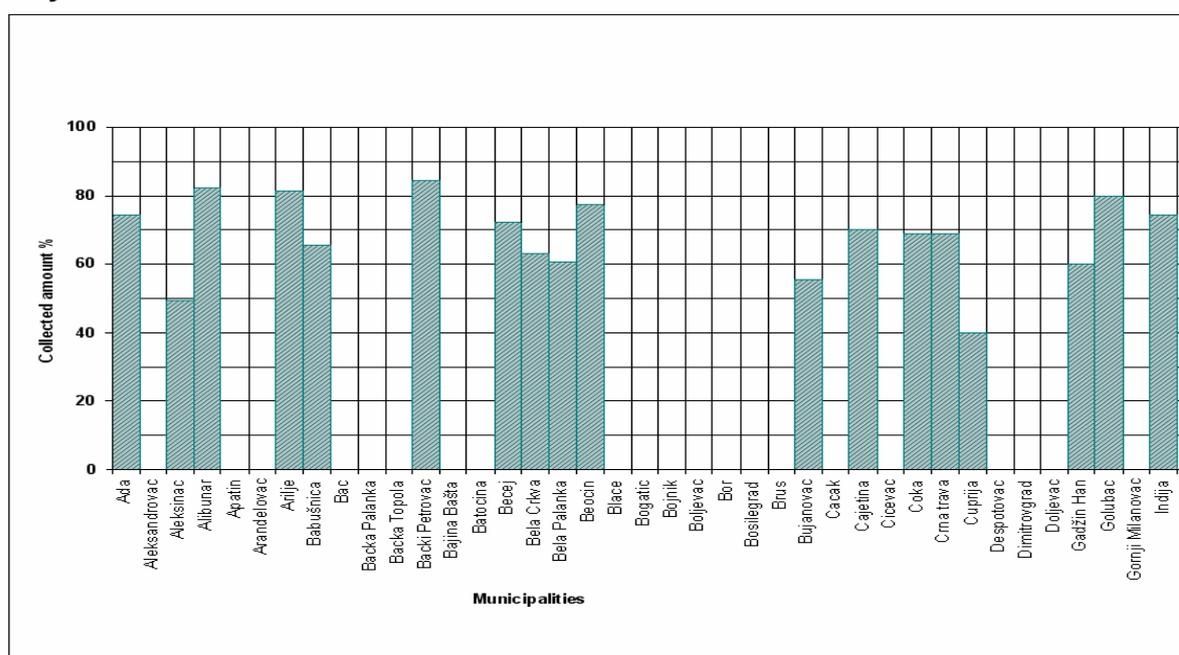




Payment Collection rate

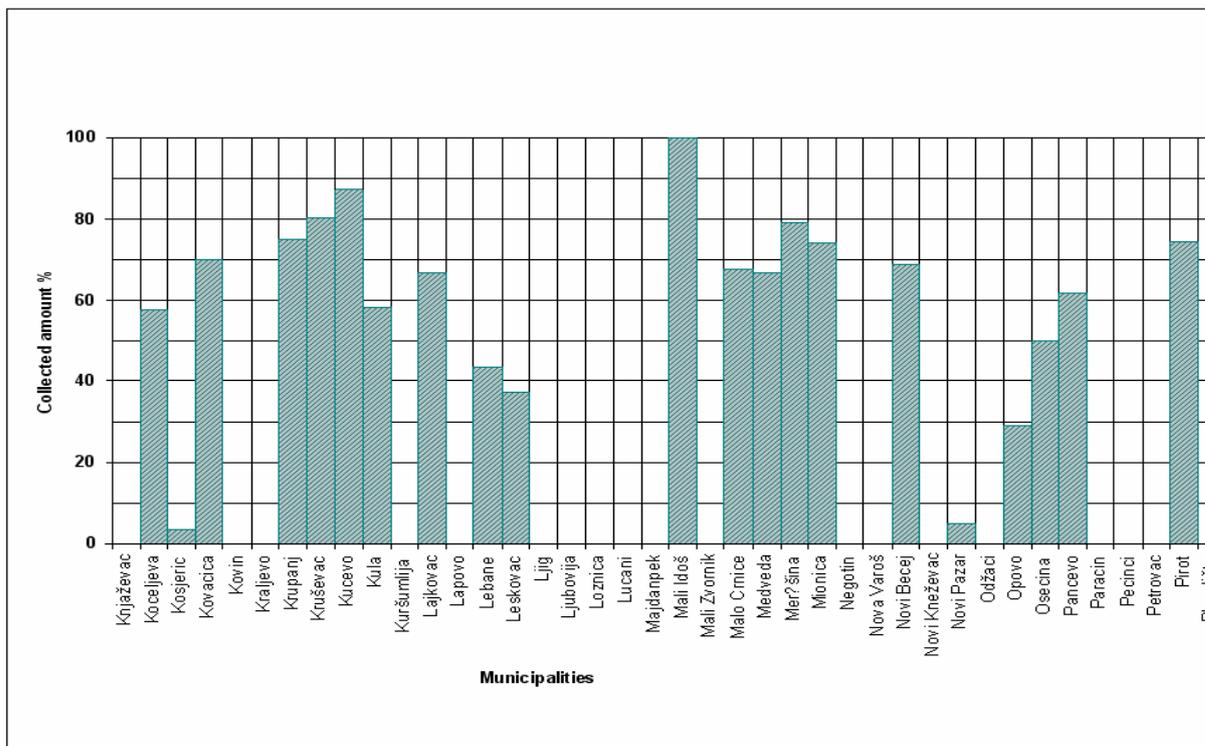
Another important benchmark is collection rates ranging from 40 % to 100 % in the municipalities in Serbia

Payment collection rate





Payment collection rate

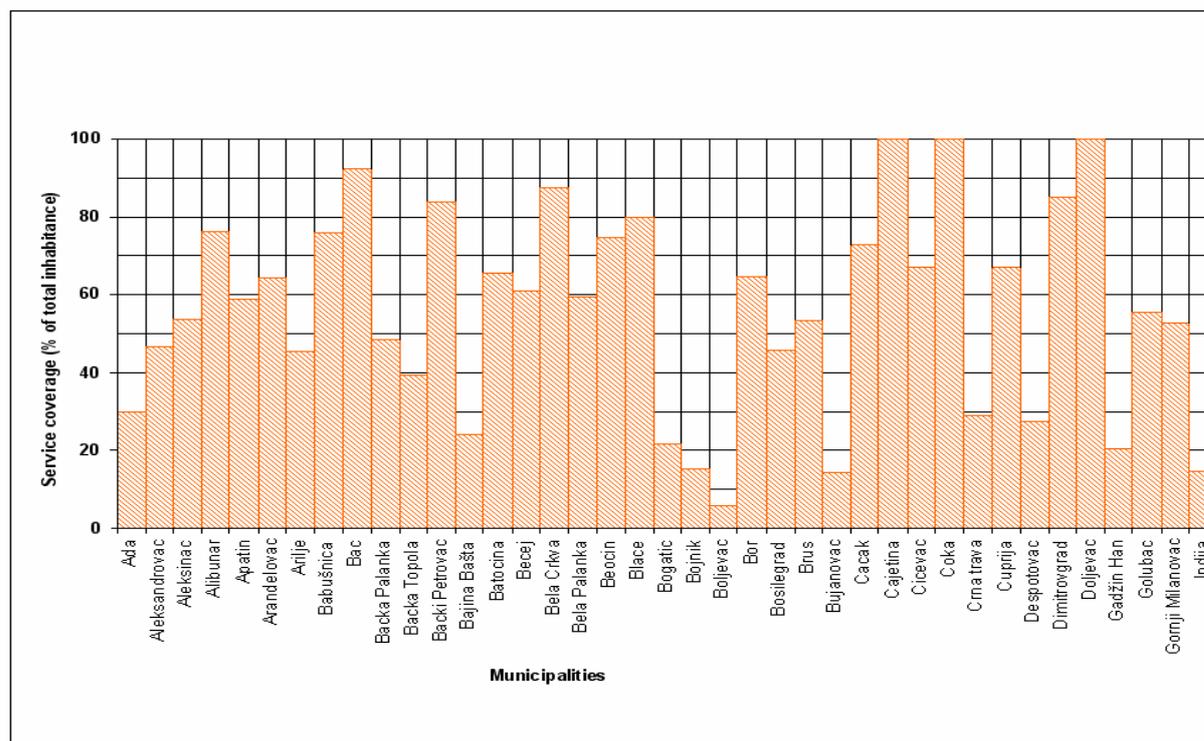




Water service coverage

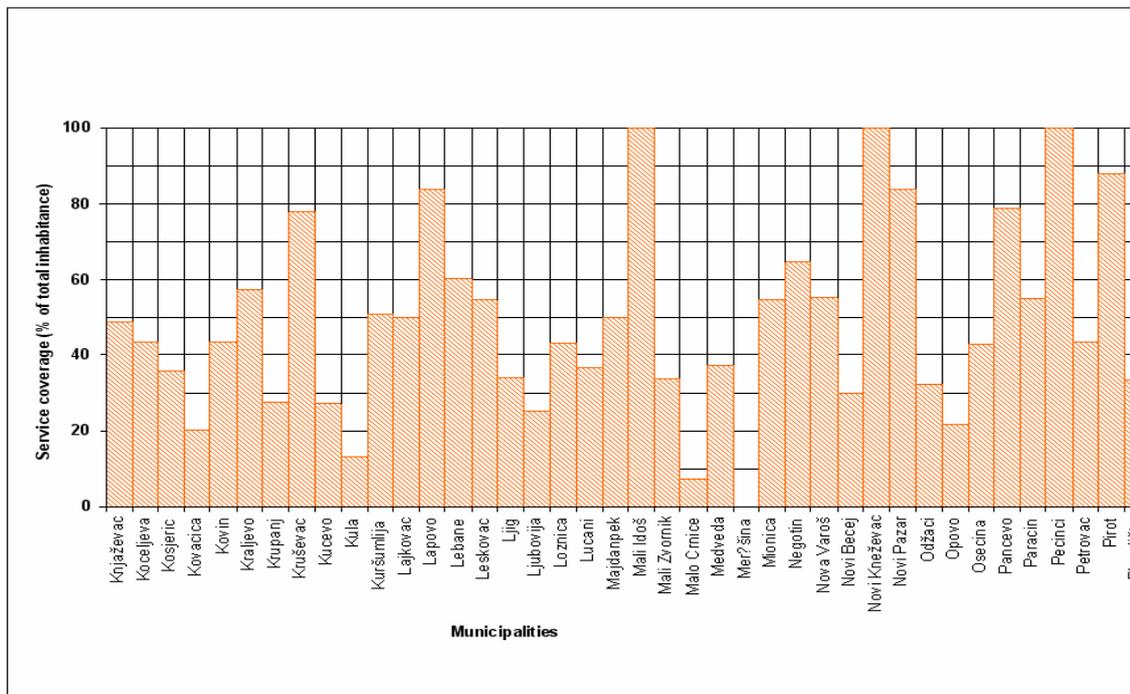
Water service coverage indicates access from citizens to water services ranging from 15 % to 100 % in the municipalities in Serbia.

Water system - service coverage





Water system - service coverage

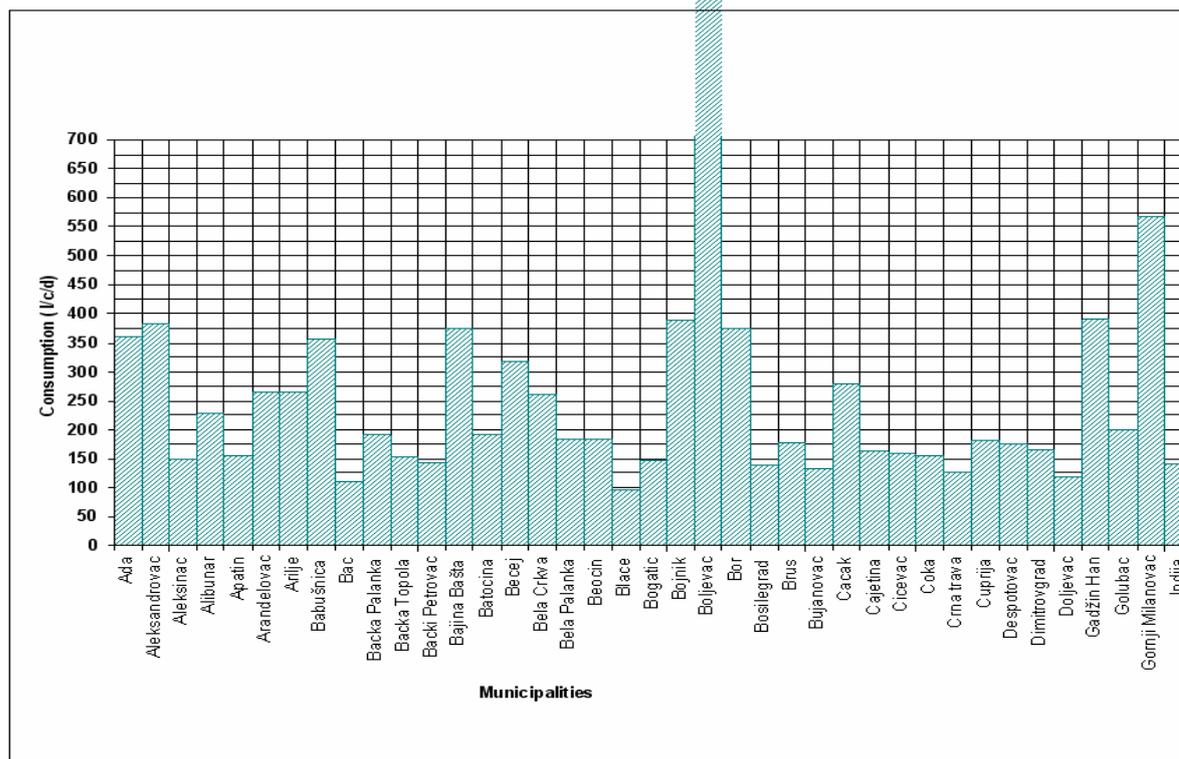




Water system consumption

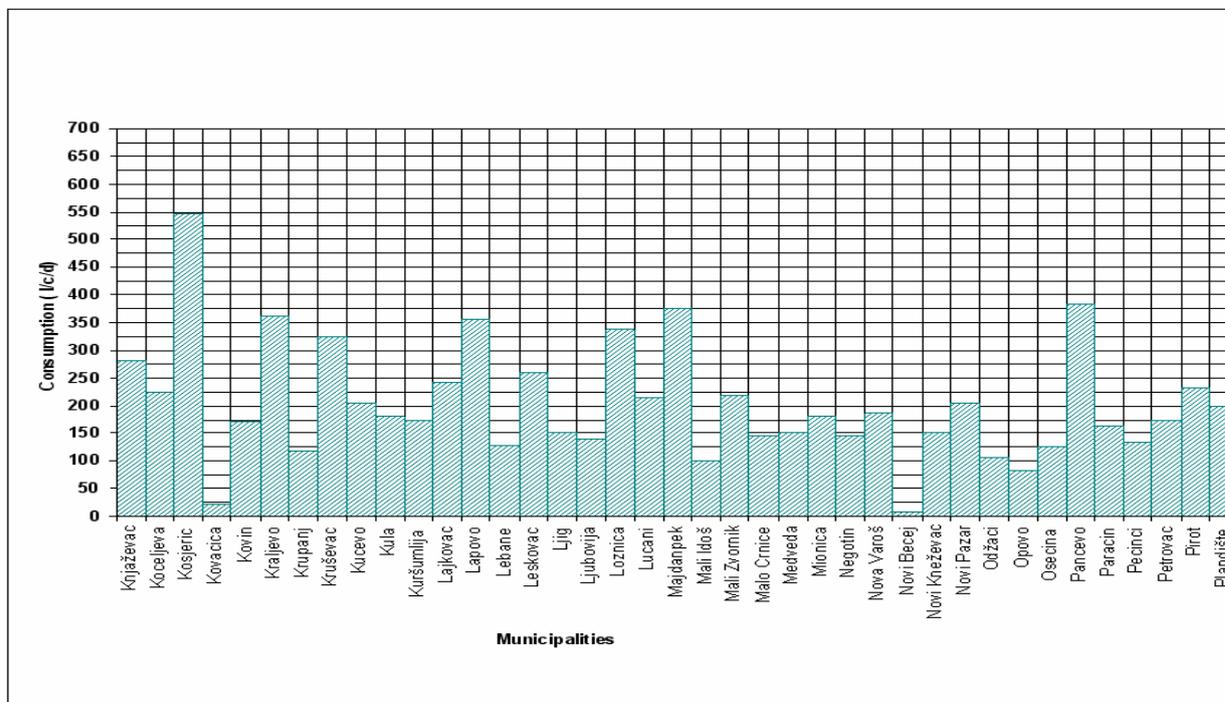
The Directorate of Water indicates a relatively high use of water which ranges between 20 to over 700 litres per capita in the municipalities of Serbia.

Water system - consumption





Water system - consumption





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Annex X

Summary of Findings and Conclusions

Round Table Meeting On the Trasformation of Public Utility Companies Belgrade 5 December 2006





1. Introduction

There is an urgent need to strengthen the performance of public utility companies, allowing them to enhance the level and quality of municipal services for water supply, sewerage, district heating and solid waste management to customers.

For this purpose the Standing Conference of Towns and Municipalities (SCTM) on the 5th of December organized a Round Table Meeting on the Transformation of Public Utility Companies in Serbia. The Meeting was attended by 45 participants from various ministries, municipalities, Public Utility Companies (PUC's) and International Financing Institutions. The Meeting took place in Belgrade in the framework of the Municipal Infrastructure Agency Support Program and was financially supported by the European Agency for Reconstruction (EAR).

2. Proceedings

In his introductory remarks, Mr. Vassilis Petrides of the EAR emphasized the need to strengthen the position of Public Utilities in order to enhance their capacity to develop and initiate high quality proposals for projects and make use of the available funds from national and international sources.

Mr. Overbeek of the Municipal Infrastructure Agency Support Program (MIASP) said that at present PUC's still face many managerial, financial and technical problems and that there is a need for the transformation of PUC's into more independent, financially strong, professional and customer oriented enterprises.

Mr. Gluscevic of the SCTM who chaired the Meeting welcomed the participants and stressed the importance of the subject of transformation of PUC's in order to improve the level of municipal services.

Mr. Hans Kok of the Municipal Infrastructure Program conducted a presentation on the Transformation of PUC.s in which he summarized the findings of an assessment of existing policies, the regulatory framework and PUC performance in three sectors: water supply and waste water, solid waste and district heating. Subsequently he presented possible strategies and instruments that could be used to support and stimulate the transformation process of PUC's.

The recommendations for possible strategies and measures presented to the Meeting were subsequently discussed in three working groups and the results of the discussions were presented to the plenary session.

3. Recommendations

Eventually the Meeting agreed on the following measures that will strengthen the position of PUC's:

1. Enlargement and Up Scaling of PUC's beyond municipal boundaries through regionalization will allow PUC's to professionalize and improve their services and increase efficiency by making use





of economies of scale. In order to realize regionalization there is a need to develop relevant sector policies and investment programs in support of this development and legislative models for inter-municipal cooperation;

2. Corporatization of PUC's, allowing them to operate as public enterprises under commercial law. This will enable participating municipalities as shareholders to extend sufficient control and at the same time allow PUC management to develop their organizations into professional service providers. For this purpose it is important to develop instruments like Service Level Agreements and Benchmarking in order to enable shareholders to monitor the level of service and the efficiency of operations.
3. Strengthen the financial position of PUC's by 1) allowing them to set adequate tariffs for high quality services and gradually achieve full recovery of operational and capital costs and 2) the transfer of assets from the national government to the PUC's, allowing the optimal use of these assets for the further development of their organizations.
4. Develop and adapt national and sector policies and regulations to provide direction and enable the above measures to be implemented at the municipal and regional level.

The Meeting agreed to request the Standing Conference of Towns and Municipalities to establish a special Working Group on the Transformation of PUC's with the support of the European Agency for Reconstruction and the Municipal Infrastructure Agency Support Program to further operationalize the above measures and put them on the political agenda with the appropriate Ministries after the upcoming elections.

