FOREIGN EXCHANGE OPERATIONS

CURRENT SITUATION

As of 28 April 2018, when the amendments to the Law on Foreign Exchange Operations (Official Gazette of RS Nos. 62/2006, 31/2011, 119/2012, 139/2014 and 30/2018) (Law) entered into force, no significant changes in the field of foreign exchange regulations have occurred.

Since the last edition of the White Book, several by-laws have been adopted and amended. In general the changes referred to opening and maintaining the funds on bank accounts abroad, regulation on foreign exchange market, currency exchange operations, etc. Second quarter of 2020 is marked by the COVID-19 outbreak which in addition to the forex operations had an impact on all other areas of business.

During 2019 Serbian business community represented through various domestic and foreign business associations (including FIC) submitted an initiative to the National Bank of Serbia (NBS) and Ministry of Finance (MF) directed towards liberalization of forex operations in Serbia. Although the NBS was of the opinion that the liberalization is not justified from the perspective of financial stability, there seem to be willingness of the NBS to consider (together with MF) some liberalization in the area of transfer of cross-border receivables/debts.

COVID-19

COVID-19 outbreak impacted the volume of cross-border transactions, but was not followed by radical legislation changes in this field. Certain technical changes to the legislation which occurred were directed mostly towards relaxation of administrative burdens in delivery of the documentation to the NBS. However, the measures and restrictions in other fields of law had the implications to forex operations and foreign investors activities in Serbia. During the state of emergency which was in force from mid-March to beginning of May 2020, almost all authorities (courts, notaries, public bailiffs, etc.) worked under a special regime (lower capacity, shortened working hours). Although the state of emergency is over, court and administrative procedures may be expected to be prolonged due to accumulated workload. During the state of emergency, the NBS and public financing institutions in Serbia (e.g. Development Fund) declared moratorium on loan and financial leasing repayments for domestic participant on the market, which moratorium was over end of June.

POSITIVE DEVELOPMENTS

During the last year there have been no material changes of the Law and/or the bylaws, and thus significant positive developments in this area have not been made. Developments are to the large extent slowed down due to COVID-19 outbreak during 2020.

REMAINING ISSUES

Despite the partial liberalisation in the field of forex operations, the current legislation remains restrictive, with the aim of protecting and preserving the macroeconomic stability.

We believe it is necessary to adapt the wording of the Law and the interpretation in practice to the approach in which prohibited operations are explicitly prescribed as such, while all other activities should be considered permitted. This principle has already been set out in Articles 3 (1) and 10 (1) of the Law, however, due to the legislative approach prescribing, in other parts of the Law, which transactions residents and non-residents may perform, the predominant interpretation in practice remains that all other unregulated activities are not in accordance with the Law. Legal transactions and the market continuously evolve, and it is neither possible nor expedient to apply a legislative technique that lists the allowed operations, while regarding the others as unpermitted. In practice, this perennial approach results in situations where certain operations, which the legislator does not seem to intend to exclude, cannot be performed due to the lack of governing norms. In addition, it is noticeable that, in certain matters, the competent authorities' interpretation narrows down the scope of application of certain rules, thereby constraining the operations of participants in the field of forex operations. However, if a list of permitted transactions is retained, we believe that it needs to be expanded wherever justified and feasible, especially when it comes to groups of affiliates, which seek to simplify financial relations within the group. Therefore, the issue of liberalisation of foreign credit and deposit operations remains open, and such liberalization is necessary to enable the provision of more sophisticated banking services, such as cash management, cash pooling and similar packages.

Practical obstacle in conducting cross-border loan transactions arises from the ex-ante reporting procedure of the NBS which is a precondition for utilization of funds by res-

ident companies. Given the purely statistical purpose of reporting, simplification of the said procedure is necessary, e.g. by introducing the obligation of ex-post aggregate reporting by e-mail, with a reduced volume of documentation or in a similar manner.

We emphasize that the issues of transfer, payment and collection of receivables based on current and capital transactions are not adequately regulated, since only Article 33 sets the rule for all types of permitted current and capital operations, but only in transfers between two non-residents. Articles 7 and 20 regulate transfers in 'realised' foreign trade and credit transactions, while similar rules are missing for all other types of transactions - for example, for receivables arising out of direct investment, guarantees, real estate, etc. The very concept of realised foreign trade is not clear, and brings into question the possibility of transfer under Article 7 when it comes to claiming an advance payment refund before the performance of the transaction. Also, the provisions on obtaining the approval of the Government for certain operations, in particular Articles 7, 20 and 33, need to be re-examined as they appear to be unnecessarily broad and restrictive, especially when it comes to the assignment of non-resident's receivables. In addition, the term "state-owned company" used in these articles is not defined and not clear and should be defined and specified so as not to include companies with indirect state capital or minority state capital (in which cases it appears inappropriate to be required to obtain approval from the Government).

Moreover, in relation to the Article 6 of the Law and the relevant by-laws, it remains necessary to liberalize the cross-border set-off of mutual receivables and debts, in accordance with the general rules of contract law. The current set-off rules are defined only for certain types of operations, while there remains a gap when it comes to other operations (e.g. real estate operations) and the interpretation in practice that these are unpermitted. Also, there is a need in practice to liberalise foreign deposit operations of residents, especially for companies that are the subject of project financing by foreign banks and international financial institutions.

Furthermore, the by-laws regarding foreign cash inflows do not fully allow the automation of international payment transactions. In order for a resident to realise foreign cash inflow, it must first provide the bank with information for statistical purposes regarding the basis for collection and in certain situations documentation for justification of the basis of collection. In its attempt at liberalisation, the NBS excluded the application of the aforementioned procedure for certain types of inflows on a single basis in the amount of up to EUR 1,000.

By amendments to the Article 23 of the Law and adoption of the relevant by-law in 2018, the Law envisaged possibilities of granting the financial credits by resident – legal entity to non-residents, as well as granting of guarantees and collaterals by resident – legal entity for obligations of non-resident under a credit transaction between two non-residents, for certain categories of non-residents (if they are from EU member states or non-resident debtor is majority owned by resident). These amendments led to certain ambiguity as to intentions of the legislator. It is not clear why the intention of the legislator was limited only to granting of guarantees and collaterals by residents only for credit transactions between non-residents, and not for guarantee transactions in terms of the Article 26 of the Law in relation to which further liberelization of the Law is still required.

Additionally, in practice the manner of granting collaterals pursuant to the Article 23 of the Law is performed in the way that granting a loan to a non-resident by a resident bank or issuance of guarantee to a non-resident bank, upon instruction of the non-resident (under a credit transaction between two non-residents), resident banks are obliged to obtain collaterals from a non-resident borrower or non-resident client, which are often of less quality compared to collaterals which resident banks could obtain from a resident/owner of concrete non-resident, which have apparent legal interest to provide collaterals for transaction of its daughter company.

Therefore the next amendments to the Law should include liberalization of this article in terms of enabling resident banks to obtain collaterals from resident/owner of non-resident under guarantee transactions between two non-residents.

Also, a resident bank finances a non-resident abroad for which it is obliged to obtain adequate collateral under the Law. In accordance with the Decision on conditions under which and manner under which resident may grant financial loans to non-residents and grant guarantees and other collaterals under credit transactions with abroad and credit transactions between non-residents, resident/owner

of non-resident in this case is not entitled to provide any collateral, given that the Law enables collateralization by resident only in case that the matter is credit transaction between two non-residents, but not in case of crediting non-resident by resident bank. This way resident banks are put into disadvantaged position against non-resident banks financing the non-resident.

Moreover, under the Article 23 and relevant by-law of the NBS, only the conditions for granting financial loans to non-residents - debtors from the EU member states have been liberalised. However, the restriction on residents to approve a financial loan to a non-resident only if it is majority owned by a resident is still applicable to non-residents outside of the EU member states. It is unclear how this change will affect entities such as international financial organizations, whose formal registered seat is neither in the EU nor outside the EU. Additionally, the discretion of the NBS to restrict individual residents from providing guarantees and other types of security for foreign loans or from granting loans to non-residents creates significant legal uncertainty. The restriction procedure itself and the moment at which the NBS may render the decision on restriction are not further defined. Furthermore, the wide scope of this discretion of the NBS applies not only to foreign loans granted by a resident to a non-resident and guarantees/securities for foreign loans, but also to guarantees/securities provided by residents for foreign loans taken by residents (which tightens the legal regime for such loans). The improvements represent the position of NBS that even banks based in Great Britain have the status of banks from the EU until the transitional period of Great Britain's exit from the EU is formally completed, in any case until 2020. And after 2020, NBS will harmonise its position regarding banks based in Great Britain with the position of EU member states and with the eventual bilateral documents that will be in effect between Serbia and Great Britain.

Finally, Article 32 of the Law allows legal entities and entrepreneurs to perform cross-border payment transactions through a payment institution and the public postal operator. At the same time, however, the Law on Payment Transactions of Legal Entities, Entrepreneurs and Individuals Not Engaged in Business Activity ("Official Gazette of RS" no. 68/2015) prescribes the obligation for legal entities and entrepreneurs to make payments through a current account opened with a bank or the Treasury Department (which indirectly indicates that payment institutions and the public postal operator are not authorised to conduct international payment operations). For this reason, it is necessary to harmonise the aforementioned law and the law regulating payment services with the amendments to the Law in order to fully enable legal entities and entrepreneurs to perform cross-border payment transactions through a payment institution and the public postal operator.

Therefore, the policy in the area of forex operations should be directed towards the further liberalisation of current and capital transactions in order to harmonise the applicable Serbian legislation with EU regulations and international standards in this area. It should also be ensured that the application and interpretation of the regulations by the competent authorities is accompanied by adequate amendments.

FIC RECOMMENDATIONS

- Adapt the wording of the Law and interpretation in practice so that prohibited operations are explicitly prescribed as such, whereas all other activities are considered permitted. (3)
- Switch to ex-post reporting of the cross-border loan transactions. (3)
- Ensure better public availability of opinions of state authorities in charge of forex operations, in particular NBS, for the consistency in application of regulations by all participants (e.g., to introduce the publication of official opinions on the regulator's website, introduce a section of responses to questions on the website, publish on the website questions and answers from consultations with commercial banks in which representatives of regulators participate, etc.). (3)

- Reconsider the wide scope of NBS' discretion to restrict a resident from granting securities or guarantees in relation to foreign loans, especially in relation to regular foreign loans and further regulate the procedure thereof, as envisaged by the by-law of the NBS which was adopted last year in parallel with amendments to the Law under the amended Article 23. (2)

- Simplify the set-off rules from the Article 6 of the Law (and relevant by-laws) for all types of current and capital transactions and allow cash pooling between affiliated parties. (2)

- Reconsider Articles 7, 20 and 33 of the Law so that the transfer, payment and collection of receivables and debts are resolved adequately for all types of current and capital transactions. (3)

- Enable foreign inflows without prior notification to the bank, as currently envisaged by by-laws governing cash inflow and outflow with abroad, subject to condition (if necessary) for such notification to be made subsequently and electronically at certain time intervals, if possible directly from the companies and not threw commercial banks (e.g. monthly, quarterly, etc.) For natural persons, enable automatic distribution of all inflows from abroad, ie without exceptions regarding the notification of the Bank on certain bases of inflow. (3)

- Further liberalisation of foreign deposit transactions of residents, especially for companies subject to project financing by foreign banks and international financial institutions. (1)

- Further relaxation of administrative requirements (e.g. delivery of documentation via email instead in hard copy) due to obstacles caused by COVID-19 pandemic. (3)