

Invitation for participation in Public Consultation

The Ministry of Finance of the Republic of Serbia invites and welcomes interested parties, including banks, investors and legal and financial advisors, to participate in a public consultation with a goal of improving the overall conditions for effective resolution of non-performing loans (“NPL”), removing obstacles to such resolution, and creation of an active NPL market in Serbia.

Copies of the document for Public Consultation (NPL Market Study – “Analysis of the existing impediments to the sale of NPLs in Serbia”, prepared by the EBRD together with KPMG and Schoenherr) can be found on the official website of the Ministry of Finance of the Republic of Serbia and the EBRD [<http://www.ebrd.com/news/events/npl-market-development.html>].

Comments should be submitted in electronic form by email to srboljub.kovacevic@mfin.gov.rs, olivera.zdravkovic@mfin.gov.rs and dino.adamovic@mfin.gov.rs, in Serbian or English language, no later than

16:00 CET on 20 May 2016. The Ministry of Finance and the NPL Working Group will consider all comments when deciding on specific actions and measures under the Action Plan to enable effective NPL resolution and market development.

1 Introduction – NPL Resolution Strategy and NPL Market Development

Acknowledging the high and persistent level of NPLs and their negative effect on bank lending and real economy performance, the Serbian authorities, with assistance from a number of international financial institutions (IFIs), have tasked a Working Group (“NPL Working Group”) to develop a comprehensive NPL Resolution Strategy, which was published in the “Official Gazette of the Republic of Serbia”, No. 72/15 and an accompanying Action Plan, that aims, among other matters, to (i) identify and remove impediments for meaningful debt resolution; (ii) strengthen incentives for viable but distressed debtors and creditors to participate in meaningful restructuring; (iii) ensure timely loss recognition; and (iv) prevent further accumulation of distressed debt in the Serbian banking system. In connection to the strategy the National Bank of Serbia (NBS) also developed its action plan. The NPL Resolution Strategy and Action Plans, when implemented jointly, should help put NPL levels on a downward trajectory.

One of the areas identified in the NPL Strategy and related Action Plan is to enable conditions for NPL (trading) market development in Serbia. In October 2015 the EBRD engaged consultants, KPMG Belgrade and Law office Moravčević, Vojnović i Partneri in cooperation with Schoenherr, to assist in preparing a comprehensive analysis identifying existing impediments for the sale of NPLs from a financial, accounting, legal, tax and practical point of view, and proposing recommendations that would resolve or mitigate the identified impediments (“NPL Market Study”).

2 Analysis of the existing impediments to the sale of NPLs in Serbia – Executive Summary

The NPL Market Study was discussed at the official NPL Working Group meetings during the first quarter of 2016.

The following areas were analyzed by the Consultants:

- Regulatory framework governing transferability of NPLs outside banking sector
- Banking data secrecy matters
- Commercial aspect - pricing gap
- Synthetic NPL sale vs. outright sale
- NPL sales and Civil procedure
- Transfer of NPLs to foreign entities
- Tax related aspects of NPL transactions
- Accounting aspects

- Transfer of collaterals
- Fresh money injection
- Related party issues linked with NPLs under restructuring / insolvency
- Group restructurings
- Adoption of a reorganization plan

2.1 Key impediments identified

The following most important impediments were addressed in the NPL Market Study:

- Obstacles of banks to process/transfer important data relating to defaulting clients (under banking secrecy definition and personal data) to potential buyers during “due diligence” phase;
- Non-assignability of retail NPLs outside of banking sector, non-assignability of performing (corporate) loans outside banking sector and prohibition of loan transfers to foreign entities;
- Strict requirements for write-off of receivables including misinterpretation that write off equals debt release and treatment of receivable write-off for individuals as their private income;
- Varying interpretations of loan loss provisioning by banks backed by inadequate collateral valuations;
- Inefficiency of mortgage re-registration process and insufficient capacity of the second instance authorities;
- Lack of technical and human capacity and experience of courts dealing with insolvency/UPPR cases;
- Lack of protection for super-seniority of new money under UPPRs / judicial insolvency reorganization;
- Systematic use of related party transactions and the deterioration of value for the creditors in large complex NPL cases;
- Regulating UPPR of a debtor as an individual company and not as a part of the corporate group by the Insolvency Act.

Additional lower priority impediments were also addressed in the NPL Market Report.

2.2 Responses of the NPL Working Group

The members of the NPL Working Group have given their preliminary responses/comments to the impediments, as identified in the NPL Market Study and, more specifically, to the recommendations for their resolution contained therein.

After assembling the responses/comments of each individual member, the NPL Working Group presented to the EBRD and the Consultants its consolidated stances on each impediment and its related recommendation for resolution, which range from full agreement on the importance of a particular impediment and recommended modality for its resolution, to partial agreement (with additional need for considerations/discussions), to complete disagreement on the importance of impediment and recommended modality for its resolution.

The NPL Working Group will assume its final stances on each impediment and related recommendation for its resolution after the end of Public Consultation, i.e. after having processed the comments received from interested parties that will participate in the Public Consultation.