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Analysis of Arrears of Public Prosecutors Offices in Serbia

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Abbreviations

SPC	State Prosecutorial Council
PPO	Public Prosecutor Office
APPO	Appellate Public Prosecutor Office
HPPO	Higher Public Prosecutor Office
BPPO	Basic Public Prosecutor Office
FMIS	Financial Management Information System
FINPLAN	Financial Planning System for budget users
MoF	Ministry of Finance
MoJ	Ministry of Justice
ZUP	Accounting system of the prosecutor's offices
BSL	Budget System Law
PFMRP	Public Financial Management Reform Program

Table of Contents

Executive Summary	1
1. Introduction	3
1.2. Overall context	3
1.3. Objectives and approach	4
2. Expenditure of selected PPOs.....	5
3. Commitment assumption practice	8
4. Arrears in the PPOs system – level, trend and structure	15
5. Main findings.....	20
Recommendations.....	21
ANNEX 1.....	23
ANNEX 2.....	25
ANNEX 3.....	27

List of Tables

Table 1. Total expenditure for investigation and postal services for selected PPOs	6
Table 2. Total expenditure for investigation and postal services for selected PPOs, per active case and per prosecutor.....	8
Table 3. Commitments for investigation and postal services in selected PPOs (annual data)	12
Table 4. Structure of arrears in selected PPOs as of June 2016.....	17
Table 5. Structure of arrears per prosecutor in selected PPOs as of June 2016.....	17
Table 6. Largest creditors as of November 2016.....	19

List of Figures

Figure 1.Process of assuming commitments (generic)	10
Figure 2.Commitments for investigation in BPPOs Novi Sad and Smederevo (monthly data) ...	13
Figure 3.Commitments for postal services in BPPOs Novi Sad and Smederevo (monthly data) ..	14
Figure 4.Structure of investigation related commitments in BPPOs Novi Sad and Smederevo ..	15
Figure 5. Term structure of arrears in PPOs	16
Figure 6.Quarterly arrears level and structure in BPPO Novi Sad and BPPO Smederevo	18

Executive Summary

- 1. This report represents the output of the analysis of arrears of Public Prosecutor's Offices in the Republic of Serbia.** The analysis was conducted on a sample of five PPOs during November and December 2016. The sample was selected based on the needs expressed by the State Prosecutorial Council that reflected the necessity to capture different PPO instances as well as PPOs with arrear levels at both extremes of the spectrum. The final sample included: HPPO Belgrade, HPPO Valjevo, BPPO Smederevo, BPPO Prokuplje and BPPO Novi Sad. The primary focus of the analysis was to address the two key sources of arrears accumulation – investigation and postal related expenditure.
- 2. We focused on a set of questions (i.e. research items) which are designed to provide comprehensive insight in the issue of arrears accumulation.** These include: assessment of the budgetary status and the overall financial management practice in sample PPOs, assessment of the expenditure levels for investigation and postal services across the sample, assessment of the process of expenditure verification and assumption of financial commitments regarding these two types of expenditures, assessment of the accounting and reporting practice around these commitments, analysis of the process of arrears management and reporting, and finally the assessment of enforced collection volumes and associated expenditures.
- 3. We found substantial differences in the process of commitment assumption regarding investigation expenditure.** Apart from the lack of clarity and guidance in expenditure verification and improper financial management IT infrastructure in place, this reflect heavily on the observed levels and the differences in levels of arrears across the PPOs. For instance, some PPOs have arrangements with courts which enable them to transfer large portions of their investigation expenditure to them after an indictment is issued. This gives them the opportunity to clear their arrears much faster than the PPOs which do not enjoy this privilege.
- 4. Another important finding of our analysis is that the investigation related expenditure levels per case vary significantly across PPOs.** We found large discrepancy in cost per case both across the whole sample and across the PPOs from the same category (i.e. instance). We found some offices paying consistently two or even three times more per case than their counterparts from the same category. These differences cannot be explained by the increase in case load and the level of complexity of cases managed by PPOs.

- 5. Our recommendations are formulated to increase transparency, protect integrity and increase financial and overall performance of Serbian PPOs.** They include: creation of a list of appropriated services and ranges of acceptable costs per case to prevent discrepancies in costs per case; enhancing provisions of the Rulebook on Charges in Judicial Proceedings to enhance investigation related expenditure verification process; establishing standardized practice of commitment assumption regarding investigation expenditure; ensuring that commitments are recorded and reported adequately to the SPC; increasing/modifying the budgets of PPOs to reflect implementation of the above reforms while regularly monitoring and analyzing arrears accumulation.

1. Introduction

1.2. Overall context

1. Serbia has suffered significant output shock following the breakout of the Global Financial Crisis (GFC). After negative 3.1 percent growth recorded in 2009, the average real growth was just above zero in the period from 2010 until 2015. As a consequence of countercyclical fiscal measures undertaken by the GoS and inherent combination of the increasing public expenditure and output stagnation, fiscal deficit figures exploded reaching 5.9, 5.2 and 6.3 percent in the period from 2012 until 2014. Considering the period from the beginning of the crisis, public debt almost doubled relative to GDP going from 34 percent in 2008 to 71 percent in 2014.

2. In an effort to tackle the challenges imposed by the worsening fiscal conditions that came as a consequence of GFC, Serbia has undertaken substantial consolidation measures supported by a three-year Standby Arrangement with the IMF. In the short term, the program focused on the control of aggregate wage and pension expenditures, improvements in tax administration, and reductions in subsidies to state owned enterprises. The Government has also begun to address longer term structural problems in the administration of the public sector, focusing on functional reviews and restructuring to create opportunities for efficiency gains. The latest review of the arrangement performed in Q3 of last year showed that Serbia remains “broadly on track” with the arrangements criteria and with most of the structural benchmarks met.

3. The effects of the consolidation actions have been encouraging. All of the key indicators are showing signs of significant recovery from the positions in the first years of the crisis. GDP growth has shifted to the positive region recording 1.1 percent growth at the end of 2015 and it is expected to sustain at similar levels in the medium term. However, Serbia’s path towards better fiscal health will depend on how much it manages its public spending to bring down its high deficit – 2017 budget comes with 69 billion RSD deficit (1.6 percent of GDP) and if offset by higher GDP growth will bring the public debt level down for the first time in past several decades.

4. One of the SBA program priorities in the coming period includes elimination of domestic arrears¹. The arrears management remains one of the key challenges as the only quantitative target that was missed under September 2016 review was the ceiling on accumulation of domestic arrears, primarily because of the arrears accumulated by the judicial sector. The set of priorities defined in the last review includes also continued reform of public administration and wage system as well as public investment management.

5. Criminal Procedure Code that was introduced in 2013 transferred the responsibility for conducting criminal investigations from courts to prosecutor’s offices. As a result, the

¹ Arrears represent overdue payments for which associated financial commitments are assumed by a budget beneficiary

PPOs took over a large number of cases from the courts . Rough estimate is that around 100,000 investigation cases were transferred. The transfer of responsibilities was not adequately followed by readjustments in the budget for judiciary and an increase in budget appropriations for prosecution services. As a result, in the period from 2013 until September 2016 prosecution offices accumulated arrears in the total of RSD 572 million. This figure constitutes around , which represents 15% of the total budget for prosecution services for FY 2017 .

1.3. Objectives and approach

6. This report provides analysis of the arrears in a sample of PPOs in Serbia². More specifically, it looks at the investigation (i.e. mandatory representation and expert witness service) as well as postal service related expenditure as the main sources of arrears³. At the more technical level, it aims at providing more solid understanding of the financial management practice across the sample PPOs which we hope will deliver better insight in how arrears actually come about and explain differences in arrears levels between PPOs. The primary objective of this exercise is to present a coherent and concise argument which would be utilized to increase transparency in the arrears management, improve financial management through strengthened internal financial control and more reliable accounting records, and most importantly enhance the budget planning process. Main questions that we aim to answer are the following:

- a) What is the level of expenditure related to investigation and postal services?
- b) How does the expenditure compare across PPOs?
- c) What is the process of assuming and recording financial commitments?
- d) What are the differences in assuming commitments, if any?
- e) What are the effects of divergent practice in assuming financial commitments?
- f) How arrears are accumulated?
- g) Are proper internal financial control mechanisms in place?
- h) Are the arrears properly recorded and reported?
- i) What share of arrears end up in enforced collection?
- j) What is the damage born by the budget because of the arrears, in financial terms?

7. The sample selection criteria were built around client's requirements and the necessity to capture the different instances of the PPOs as well as "good" and "bad" examples across the whole network of PPOs in terms of the most recent level of arrears. The final sample analyzed included HPPO Belgrade, HPPO Valjevo, BPPO Smederevo, BPPO Prokuplje and BPPO Novi Sad. The initial requirement was to include two of the higher PPOs versus three BPPOs. Joint decision was made to include the HPPO Belgrade as the largest among the HPPOs

² Final list of PPOs to be included in this analysis was finalized in cooperation with the State Prosecutorial Council.

³ Other reasons for incurrence of arrears include late payments for utility bills, telecommunications, urgent repairs, stationery, etc.

and the one with the highest level of arrears in the whole network⁴ in absolute terms. HPPO Valjevo was included as an example of an institution with presumably sound financial management practice. Among the BPPOs the selection was made based on the ratio of arrears per prosecutor⁵ and the size of the office. Final sample of BPPO included Novi Sad as the office with relatively large number of prosecutors (i.e. 26 versus the average of 7) and low level of arrears, as well as BPPO Prokuplje and BPPO Smederevo as mid-size offices with relatively high level of arrears per prosecutor.⁶ Relevant data were collected from the SPC and the sample PPOs through emails and interviews. Total arrears accumulated as of September 2016 for all (basic and higher) PPOs are shown in Annex 1.

8. The rest of the report is structured as follows. Section 2 discusses the expenditure of selected PPOs and provides a general context of PFM in terms of arrears. Section 3 discusses the differences in commitment assumption among the sample PPOs. Section 4 analyzes the level, trend and structure of arrears. Section 5 summarizes the main findings while Section 6 lists recommendations for improving current financial management function of the PPOs in Serbia.

2. Expenditure of selected PPOs

9. Budgetary status of PPOs is somewhat undefined given that they act as a direct budget beneficiaries while at the same time they rely on the SPC and MoJ for appropriation management and control. PPOs are independent in terms of budget execution (i.e. entering payment orders in FMIS), however the SPC and MoJ acts as an intermediary between the central budget authority – Budget Sector of the MoF and PPOs in terms of determining initial appropriations, their in-year virement and control. Financial planning function is also combined with the SPC such that PPOs prepare their three month rolling spending plans and enter it into FINPLAN whereas SPC aggregates these plans and works together with Treasury Administration in determining the monthly spending quotas.

10. Based on the Treasury Administration plan for reduction of IBBs the PPOs along with courts were included in the first phase of the FMIS roll out to indirect budget beneficiaries. Recently developed PFMRF envisages gradual extension of the FMIS coverage to IBBs by including all of them in the budgetary accounting and reporting framework. In the next stage of the process which is scheduled to be completed by the end of 2018, the rest of the IBBs

⁴ Its reported arrears as of September 2016 were RSD 158.6 million

⁵ Number of prosecutors were decided based on the Decision on the number of deputy public prosecutors (Official Gazette, 106/2013, 94/2015, 114/2015 and 80/2016) and reflects the size of the population living on the territory covered by the respective PO.

⁶ When sorted strictly based on the criteria of arrears-to-prosecutor ratio, all BPPOs from Belgrade (all three of them) turned most successful – they have zero arrears. However, we wanted to avoid having HPPO and BPPO from the same city. Also, the least successful were BPPOs Ruma and Brus, but these offices were not considered representative because they were too small - with one and four prosecutors, respectively.

which were previously subordinate budget beneficiaries of the Ministry of Justice (mainly prisons) will be included in the FMIS.

11. It is not possible to track the flow of commitments and impose strict expenditure controls over budget beneficiaries that are out of the scope of FMIS.. Previously, holding a status of anIBB, PPOs were regularly transferred money to their own transactional accounts held at the Treasury and were making payments without any in-year budgetary control. There were also no technical prerequisites to control for financial commitments made by PPOs. It was only at the end of the fiscal year when the expenditure of PPOs, as of any other IBB, was checked against their financial plans through self-made budget execution reports sent to the TRE and Ministry of Justice⁷. The quality of these reports was largely dependent on accounting practices which were seldom unique and standardized across different offices. These circumstances imposed large fiscal risks as there was no mechanism in place to control the in-year expenditure and financial commitments made by them which made it possible for them to incur arrears.

12. Investigation and postal service related costs vary significantly across the sample. Table 1 below shows the aggregate expenditure levels for the two types of costs analyzed in this report, in the period between January 2014 and June 2016. The differences between different PPOs seem to be in line with the variation in size of the territories they cover (e.g. BPPO Novi Sad versus BPPO Prokuplje). In additions, there is a correlation between the costs of procedures in different levels of PPOs where the complexity of cases handled by an HPPO is much higher than that of the BPPO, as prescribed by the Criminal Procedure Code (e.g. HPPO Belgrade versus BPPO Novi Sad).

Table 1.Total expenditure for investigation and postal services for selected PPOs

PO	2014		2015		2016	
	investigation costs	postal costs	investigation costs	postal costs	investigation costs	postal costs
HPO Belgrade	43,296,560	594,383	79,599,907	428,219	22,841,416	341,079
HPO Valjevo	3,144,844	145,355	4,190,793	194,384	1,493,915	103,569
BPO Novi Sad	8,613,905	1,373,983	8,102,941	1,587,581	4,278,171	654,194
BPO Prokuplje	3,803,320	565,700	4,346,439	540,951	2,272,961	201,880
BPO Smederevo	3,279,224	300,569	5,444,388	588,697	1,363,635	189,399

source: Budget execution Reports and WB calculation

⁷ Before introduction of the SPC, their “superior” direct budget beneficiary in charge of managing their budget matters

13. Expenditure levels are increasing from the introduction of the prosecutor led investigations in 2013⁸. This trend is a result of the following: On one hand, there is a load of cases which was taken over from courts once the investigation process started being managed by the PPOs. For instance, BPPO in Novi Sad took over around 9,000 cases at the beginning of 2014, while this figure stood at around 1,500 for BPPO in Smederevo. On the other hand, there is an increasing trend in new cases coming in. Official data collected by the SPC show that for instance HPPO Belgrade had 13,380 new cases in 2015 versus 12,411 in 2014 (increase of 7.8%)⁹. With previous year cases being rolled over to the next year going up because of the initial load and the increasing number of new ones, the number of active cases is reaching higher and higher figures every year.

14. Increase in the investigation and postal service related expenditure level cannot be attributed only to increased number of active cases. The rate of increase in the number of open cases going from 2014 to 2015 is 13.2% (i.e. 53,547 versus 47,320 active cases) while the aggregate increase in investigation and postal service related expenditure is as much as 61.3% (RSD 105 mil versus RSD 65.1 mil). Highest increase of 83.4% was seen in HPPO Belgrade (RSD 80 mil versus RSD 44.9 mil). But even if HPPO Belgrade was left out, the percentage change of the expenditure is still higher than the increase in the number of active cases – 17.8% more expenditure against 13.2% of more cases handled. This indicates that the budgets are increasing every year so the debts (i.e. arrears) accumulated in the years when the budget was not sufficient can be settled.

15. Expenditure differences are striking when observing costs per active case and costs per prosecutor. Table 2 below is a reformulation of the aggregate expenditure shown in Table 1, only normalized to reflect case load and number of prosecutors to ensure comparability. There are differences both across and within different categories of PPOs (i.e. higher versus basic). HPPO Belgrade recorded 2.5 to almost 3 times higher expenditure level than HPPO Valjevo.

16. One reason for such a stark difference in can be attributed to complexity of cases managed by the HPPO in Belgrade. The HPPO Belgrade is managing relatively more complicated cases that require more time to complete and involve more complex and thus more expensive expert witness services and larger volume of mandatory representation by lawyers, compared to those managed by HPPO Valjevo.

17. The same pattern is observed with the BPPOs. Within this group, BPPO Prokuplje is a frontrunner with more than RSD 953 costs per case¹⁰ compared to RSD 409 and RSD 519 seen in

⁸ Data for 2016 cover only the period from January until June

⁹ HPPO Valjevo had a sharp increase of almost 42% in 2015 (2,483 versus 1,755 cases) while BPPO Novi Sad and BPPO Smederevo experienced a less dramatic upswing of 7% and 1.5% respectively. BPPO Prokuplje retained roughly the same number of cases in 2015 compared to 2014 (2,637 versus 2,665 cases)

¹⁰ Number of active cases includes large share of cases which are dropped at the beginning with zero direct costs

Novi Sad and Smederevo, in 2014. The difference persists through the entire observed period, and ranges from 132% to 143%, when compared to BPPO Novi Sad. When looking at the costs per prosecutors the disparity is even more pronounced. The extent of the difference between BPPO Prokuplje and BPPO Novi Sad reaches almost 300%, while when compared to BPPO Smederevo the maximum difference is reached in 2015 at the level of 60%. It is important to note that the difference between BPPO Novi Sad and BPPO Smederevo are just as outstanding as when comparing Novi Sad and Prokuplje, with the latter having much higher expenditure levels based on both criteria.

Table 2. Total expenditure for investigation and postal services for selected PPOs, per active case and per prosecutor

PO	2014		2015		2016*	
	costs per active case	cost per prosecutor	costs per active case	cost per prosecutor	costs per active case	cost per prosecutor
HPO Belgrade	3,063	1,082,414	4,879	1,851,161	1,181	531,196
HPO Valjevo	1,723	1,048,281	1,638	1,396,931	592	497,972
BPO Novi Sad	409	374,518	366	368,316	205	178,257
BPO Prokuplje	953	1,267,773	940	1,448,813	498	757,654
BPO Smederevo	519	819,806	690	907,398	173	227,273

source: Budget execution Reports and WB calculation

*Budget execution data for 2016 are for period Jan-Jun, while data on caseload per PO are estimates based on earlier years

3. Commitment assumption practice

18. Arrears are a consequence of accumulation of financial commitments which exceed financial capacity of the budgetary user as defined by its budget appropriations. Commitment control is a core financial management function and most countries exercise automatic controls over assumption of commitments which exceed the financial limits set by the budget. This is done by either imposing a requirement of performing an encumbrance (i.e. appropriation reserve) prior to assuming the commitment, or at least at the very moment of assuming the commitment.

19. In the past three years there has been significant legislative effort by the Government to bring arrears under control through increased control of commitments. The Law on Deadlines for Payments in Commercial Transactions provided a schedule for reduction of arrears. It included only transactions involving commercial entities in 2012 but has been amended to include the public entity-to-public entity transactions as well in 2015. The law enabled legal repercussions for failing to meet financial obligations of public entities. The implementation of the law required creation of an electronic Registry of Settlements of Pecuniary Commitments (RINO)

in order to improve the quality of information on commitments IBBs, while FMIS would collect this information for the DBBs.

20. However, commitment control remains a major challenge imposing high risk of arrear accumulation. While completeness of the commitment information collected through FMIS and RINO is unclear, both systems record only the commitments which are already assumed as the legislative framework does not allow for any form ex-ante control over this process. Specifically, the budgetary users are not automatically prevented from assuming commitments over the limits prescribed by their approved budgets, as no pre-approval of any form is required from budget authorities in order to assume that commitment (i.e. enter into a contractual obligation with financial repercussions).

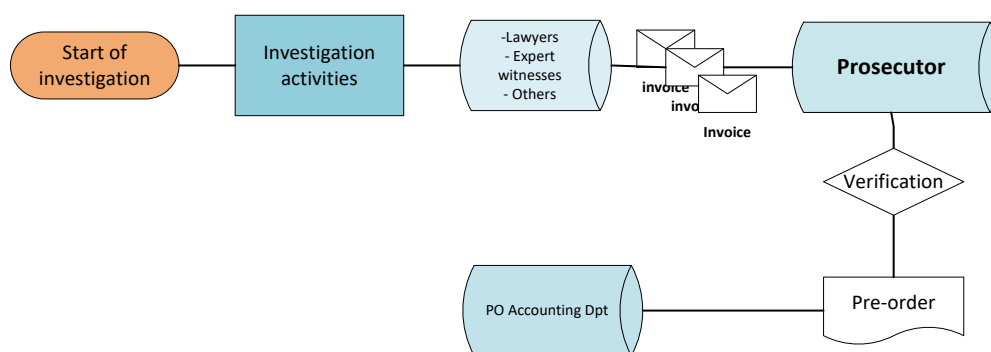
21. Current systems are not geared towards preventing arrears accumulation. RINO system works with no direct link to the budget management as it does not prevent assuming commitments which are not supported by sufficient budget funds nor does it perform encumbrance once a commitment is entered into the system. Although FMIS as the budget execution system operates with budget appropriations, the commitments entered into the system also do not trigger encumbrance. One of the obvious reasons is that commitments often have multi-year perspective and FMIS does not support multi-year commitment control as it works only with current year appropriations.

22. In case of PPOs, commitments are recorded in several parallel ways while the FMIS is not of them. In terms of the commitment control PPOs can be considered DBBs as they process their payment orders directly through FMIS. However, as confirmed by all of the interviewed chief accountants from the five PPOs, FMIS is not used for recording the commitments at all. The most complete record is kept in the notebooks of the accountants. In most cases, this evidence is supported by a spreadsheet for easier analytical interventions. And finally, commitments are kept as “accounts payable” in the accounting records of PPOs supported by ZUP (i.e. the accounting software), but it remained unknown to which extent the completeness of this type of record compares to the first two ones in all of the sample PPOs.

23. The only formal way for recording commitments is ZUP, however it does not seem to be able to provide enough analytical tools for effective monitoring of commitments. For instance, the software does not support the option of tracking commitments by the type of associated expenditure and provide immediate breakdown into those incurred by expert witnesses and lawyers. Also, it is not integrated with the FMIS at all which implies that each payment order has to be generated directly in the FMIS and then manually recorded in the accounting software (ZUP) to remove the commitment from the list of accounts payable.

24. The commitment for investigation related and postal services are assumed once a pre-order from a prosecutor managing a particular case reaches the accounting department of the PPO. Figure 1 below presents map for this procedure. The beginning of procedure is marked with the delivery of services by an expert witness or a lawyer¹¹. Upon delivery of services, both entities submit an invoice¹² with detailed breakdown of incurred expenditures and associated fees which are determined by the Rulebook on Charges in Judicial Proceedings and the Lawyers' Tariff. The process continues with the prosecutor managing the case verifying these expenditures by checking whether they comply with the provisions of the above mentioned pieces of regulation and whether they fit to what could be called "experience-based" expectation in terms of the particular service. The prosecutor then issues the pre-order¹³ with all payment details (name of the entity/person, bank account number, amount of net fee, taxes and contributions, etc.) which serves as a basis for creating a payment order in the FMIS by the financial department.

Figure 1. Process of assuming commitments (generic)



25. Lack of clear guidance and existence of different practices in accepting commitments results in significant variations between the PPOs. Considering the lifetime of a criminal case (i.e. from when the crime is committed, to arrest and investigation, eventual indictment and trial), the point when the pre-order from deputy prosecutor for payment of used services reaches the accounting department varies significantly going between the PPOs.. In BPPO Smederevo, the pre-order is sent to the accounting department immediately after the verification of the invoice in the investigation process. On the other hand, the BPPO in Novi Sad the same process is more

¹¹ Or any other entity providing support services in the investigation process. Such as: Ministry of Interior, different Public Utility Companies, translators, etc.

¹² The invoice contains usual elements: names of the parties involved (PPO and the name of the lawyer/expert witness, amount due broken down by types of services, associated social contributions and taxes, bank account details, date and location.

¹³ Starting from January 2015, HPPO Belgrade is issuing an accompanying act (i.e. decision) which, by their interpretation, has legal power in the eventual enforced collection process as opposed to the pre-order alone.

complex and selective. Namely, in case when there is no indictment, all of the commitments coming from expenses incurred in the process are assumed only at the end of the investigation. If an indictment is issued, commitments are assumed at the end of the trial. If a person is found guilty, the commitments are assumed by the court managing the trial procedure. Recently, when found guilty, the person is required to compensate both the PPO and the court for all the expenses in cases when the financial status of the person allows it.

26. However there are instances when certain commitments are assumed regardless of how investigation process will end. This is primarily for services of expert witnesses which are scarce and with complex types of expertise. Although there is subjectivity and selectiveness in payments, this practice could be justified considering that these expert witnesses would avoid providing their services since they would have to wait for the whole process (including the trial) to end which can take several years in some cases. Further, in case of HPPO Belgrade, the commitments coming from the invoices sent by expert witnesses are assumed just as in case of BPPO Smederevo – immediately after they are verified. While the invoices sent by lawyers for mandatory representation are processed at the end of the investigation process and commitments are then assumed regardless of whether an indictment is issued or not. Finally, the situation in HPPO Valjevo and BPPO Prokuplje was not sufficiently clarified, but the level of arrears of this PPO suggests that the practice could be the same as in BPPO Smederevo with the pace of assuming commitments being higher than in Novi Sad and Belgrade.

27. The process of assuming commitments is governed by the article 261 of the Criminal Procedure Code. This article regulates the area of expenses incurred in the investigation and trial process, but with insufficient clarity. First paragraph of this article lists all possible types of expenditure including the “award” prescribed for expert witnesses and lawyers along with other expenditure such as travel costs, material cost and similar. The “award” is the main source of expenditure in the investigation process and constitutes 90 to 100 percent of total expenditure as expert witnesses and lawyers in most cases do not even ask for the travel expenses and material costs if they are not significantly large. Second paragraph of this article says that other costs are paid in advance (i.e. before the end of the process) by the “institution managing the process”, while it does not say that the “award” should be paid up front leaving unnecessary room for different interpretation. While it is unclear who is the “managing institution” in case when the process end up in trial (i.e. when indictment is issued), it is also unclear whether the advance payment should be made in advance of the end of investigation or the whole process – including trial.

28. Differences in assumption of commitments among PPOs are a consequence of diverse interpretation of the article 261 of the Criminal Procedure Code. Interpretation of BPPO Novi Sad which is agreed with the Basic Court in Novi Sad is that there should be no advance payments of the “awards” to expert witnesses and lawyers, while the “managing institution” (and thus the obligor) is the PPO in cases when no indictment is issued, while the “managing institution” is the

court in cases when indictment is issued. This interpretation is supported by decisions of the Supreme Court number 1030/2015 from 08.12.2015 and 729/2014 from 22.10.2014 resolving the dispute between public attorney and expert witnesses and lawyers on who is responsible for settling expenditures in legal processes. BPPO Novi Sad thus manages to transfer very large portion of its investigation expenses to the Basic Court Novi Sad and at the same time postpone its commitments until the end of the investigation process. On the other end, BPPO Smederevo which assumes commitments much faster than BPPO Novi Sad, interprets this article in completely opposite way so the commitments coming from invoices containing “awards” for expert witnesses and lawyers are assumed “as-they-come” - much before the end of the prosecution process and regardless of whether indictment is issued or not. If some of the investigation related expenses are not paid before indictment reaches the court, the court rules that those should be settled by the BPPO Smederevo. Detailed commitment assumption process flowcharts for BPPO Smederevo, BPPO Novi Sad and HPPO Belgrade are given in Annex 2 of the report.

29. This is causing much variation in the level of investigation related commitments assumed by PPOs, while postal service commitments seem to reflect the difference in size of the offices. Table 3 below shows the level of commitments for investigation and postal service related expenditure for the period starting from January 2014 until June 2016 for those BPPO that made these data available - BPPO Novi Sad and BPPO Smederevo. We can see that the level of commitments for these two offices are very much similar through the entire period, while the difference in their case load and number of prosecutors is very significant – BPPO Novi Sad manages on average 21,300 cases per year and has 24 prosecutors while BPPO Smederevo manages almost three times less cases and has six times less prosecutors – 6 prosecutors are managing 7,300 cases on average annually.

Table 3. Commitments for investigation and postal services in selected PPOs (annual data)

PO	2014		2015		2016	
	Investigation	Postal service	Investigation	Postal service	Investigation	Postal service
Novi Sad	8,262,992	1,308,746	10,086,092	1,352,444	8,400,366	651,033
Smederevo	6,354,864	300,569	10,263,104	571,228	8,172,842	244,077

source: budget execution reports and author's calculation

30. It seems that the commitment practice observed is unique for every PPO and does not apply to other PPOs from the territory under authority of the same APPO. Since commitment data were only available for the sample PPOs, we analyzed the level of arrears (which should efficiently proxy for the level of commitments) of BPPOs on the territory of APPO Novi Sad (to which BPPO Novi Sad belongs) and compared it those from the territory of APPO Belgrade (to which BPPO Smederevo belongs). We found no significant overall difference – average arrears

per prosecutor among BPPOs of APPO Novi Sad (excluding BPPO Novi Sad) were RSD 1.12 million while those of BPPOs on the territory of APPO Belgrade (excluding BPPO Belgrade and BPPO Smederevo) were RSD 1.18 million. It follows that the commitment assumption practice is a consequence of arrangements a particular BPPO has with the responsible court (Basic Court in Novi Sad and Basic Court in Smederevo in our case).

31. There is very high positive correlation in the trend of incurring commitments related to investigation expenses in BPPO Novi Sad and BPPO Smederevo, while no seasonality is observed. Figures 2 and 3 below show the trend in investigation and postal service commitments for the two BPPOs. We can see that the two lines move together for most of the time with BPPO Novi Sad having higher commitments for postal services for the entire period while the situation varies with regard to investigation expenses – Novi Sad currently has slightly higher commitment level while for the most of 2015 they were kept below those of Smederevo. End of 2014 was marked with very high levels of assumed commitments in both PPOs, and while it was stabilized at the level of about RSD 1 mil during 2015, it started accelerating in the first half of 2016.

Figure 2. Commitments for investigation in BPPOs Novi Sad and Smederevo (monthly data)

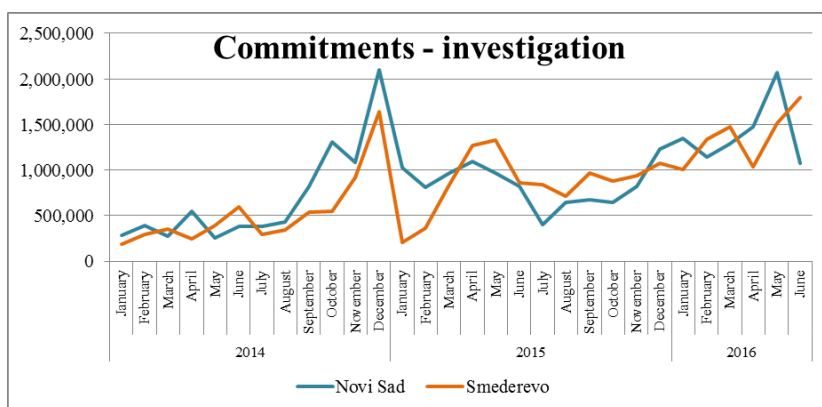
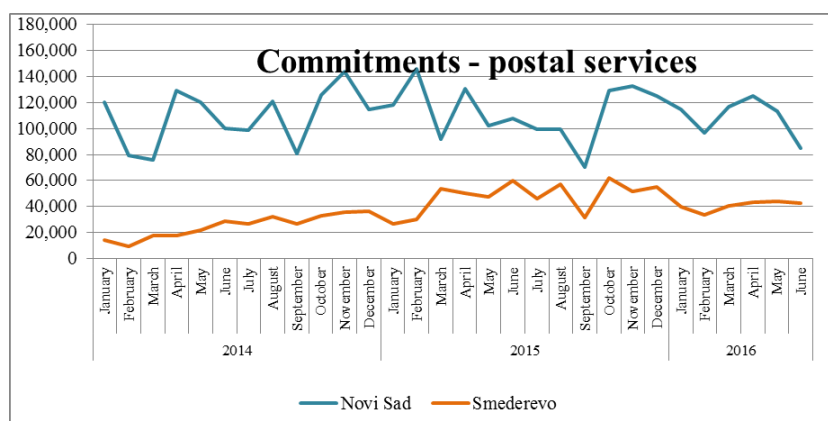
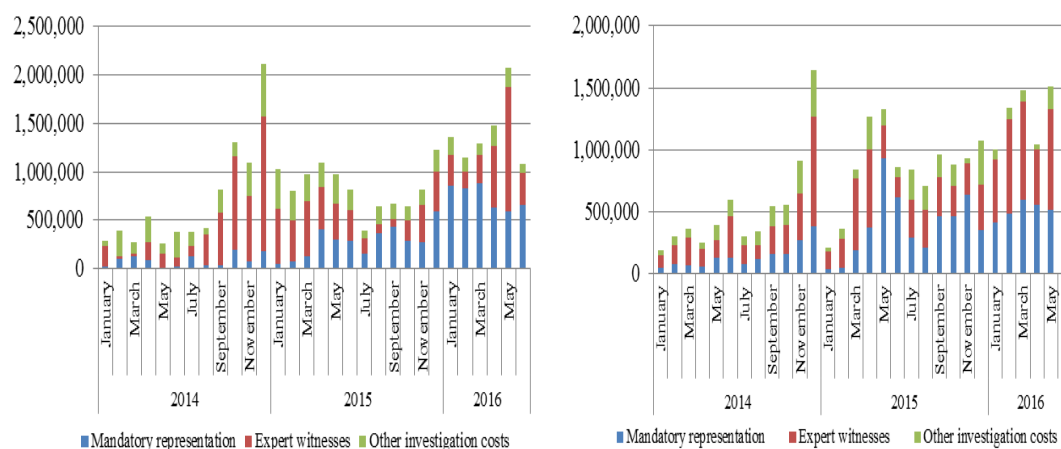


Figure 3. Commitments for postal services in BPPOs Novi Sad and Smederevo (monthly data)



32. Increase in the overall level of investigation commitments is mostly the consequence of increasing commitments related to mandatory representation in BPPO Novi Sad and Smederevo. Figure 4 below reveals the structure of investigation commitments for these two BPPOs. While the “other costs” and “expert witness” categories share is kept relatively stable with some variations throughout the period, mandatory representation commitments (marked with blue) are increasing significantly. Although we have seen that the practice of assuming commitments varies significantly it still applies to an average (general) case. This process is still not fully automatized in the sense that service providers (i.e. expert witnesses and lawyers) know exactly the point in time when their invoice will become payable. Together with the lack of internal (ex ante) and budgetary inspection (ex post) controls and the opportunity to make case to case exceptions (primarily for scarce expert witnesses), this leaves room for individual lawyers and expert witnesses and their respective associations to apply pressure on PPOs to assume financial obligations so they can get paid. Hence, the observed increasing trend may be explained by increasing pressure from Lawyers association on PPOs to assume these financial obligations. This intuition somewhat suits the data observed in Novi Sad as the PPO with “tight” commitment assumption practice and Smederevo as much less strict in this sense – the share of mandatory representation in investigation related commitments in Novi Sad was on average 16% in 2014 and then it went up by 20% both in 2015 and 2016 reaching 35% and 56% in these years, while the rate of increase in Smederevo was not so high – the share was 26% in 2014, went up to 40% in 2015 and reached 43% in June 2016.

Figure 4. Structure of investigation related commitments in BPPOs Novi Sad and Smederevo

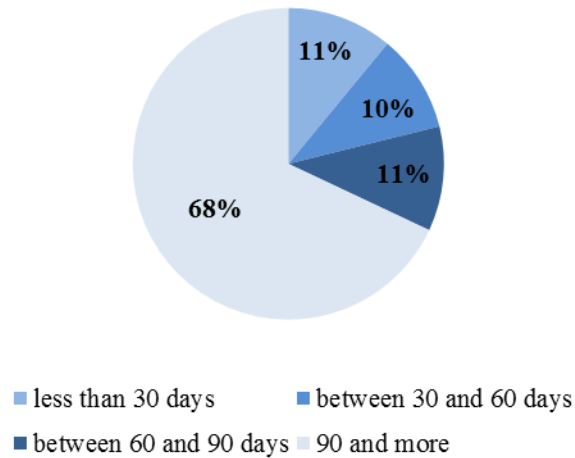


33. The observed differences in commitment assumption practice across PPOs do not only reflect on the level of commitments but naturally also on the expenditure levels and arrears, thus distorting the entire financial landscape of the PPO network. As we could see above, there is a high disproportion in size between BPPO Novi Sad and BPPO Smederevo (on average 3 times more cases and 4 times more prosecutors in Novi Sad) but this is not reflected in their expenditure levels. Smederevo has consistently higher expenditure level both per case and per prosecutor (Table 2), while it has similar level of commitments related to investigation (Figure 2). While Smederevo has the same level of commitments as Novi Sad, its level of expenditure in absolute terms although disproportionate is not quite as high as in Novi Sad (Table 1). This is explained by much higher level of arrears (unsettled commitments) observed in BPPO Smederevo versus those of BPPO Novi Sad, as we will see in the next section.

4. Arrears in the PPOs system – level, trend and structure

34. Arrears in the whole PPOs system (including basic, higher and appellate PPOs) were RSD 572 million as of September 2016. While APPOs barely have any arrears, HPPOs had RSD 284 million while BPPOs had RSD 286 million in arrears. Term structure of the arrears is such that a very large portion (68%) of arrears is older than 90 days, while the remaining portion is equally split to those bills which are overdue for less than 30 days, between 30 and 60 and between 60 and 90. Figure 5 below shows the details of the structure. This data is collected on a quarterly basis by the SPC. However, the query based on which data is collected is not structured to capture type of expenditure behind the arrears, but only the overall figures and the term structure of arrears.

Figure 5. Term structure of arrears in PPOs



35. Arrears observed in the sample PPOs reflect the differences in their commitment assumption procedures. Tables 4 and 5 below show the overall level of arrears and arrears per prosecutor for the five sample PPOs. We can see that BPPO Novi Sad has by far the lowest level of arrears per prosecutor, while BPPO Prokuplje, for which detailed data was not made available, has almost RSD 3.5 million of arrears per prosecutor. At the same time BPPO Smederevo maintained the level of RSD 2 million of arrears per prosecutor. Almost 28% (158 out of 572 million) of total arrears are made by HPPO Belgrade. Its arrears are dominated by the category of “other investigation costs”.

36. Current arrears for investigation significantly exceed annual budgets for these expenditures. When comparing the average expenditure incurred in 2014 and 2015 shown in Figure 1 above with arrears data, we can see that the ratio of annual expenditure for investigation and its current arrears for HPPO Belgrade is 2.61, in case of BPPO Smederevo it is 2.58, in case in case of BPPO Prokuplje it is 2.55, while in HPPO Valjevo the ratio is at 1.18. BPPO Novi Sad is the only office with the ratio lower than 1. At the level of the whole sample, this ratio is 2.28 which means that, assuming no further arrears, there has to be a 230% increase in the annual budget for investigation to settle the arrears of these PPOs.

37. There is a difference between arrears incurred for mandatory representation and expert witness services among PPOs of the same category. For instance, HPPO Valjevo has almost twice as much arrears for expert witness service compared to mandatory representation (RSD 3 million compared to RSD 1.6 million), while this ratio is reverse in case of HPPO Belgrade (RSD 7.6 million versus RSD 17.9 million). Assuming that the nature of cases of these HPPOs is similar, it seems reasonable to expect at least comparable level of arrears for these types of investigation related expenditures.

38. This may point to some subjectivity in the order of settling arrears. Previously it has been mentioned that some PPOs rationalize when paying their bills in order to maintain good relationships with certain expert witnesses whose expertise is scarce and needed frequently by the prosecutors.

Table 4. Arrears in selected PPOs as of June 2016

PO	Mandatory representation	Expert witnesses	Other investigation costs	Postal service costs	Total
Beograd	17,933,505	7,603,995	133,051,515	0	158,589,015
Valjevo	1,567,500	3,058,408	329,610	0	4,955,518
Novi Sad	2,792,625	2,377,346	757,443	0	5,927,414
Prokuplje	10,272,566			77,353	10,349,919
Smederevo	4,754,615	5,428,441	1,399,376	54,678	11,637,110

source: POs quarterly arrears report

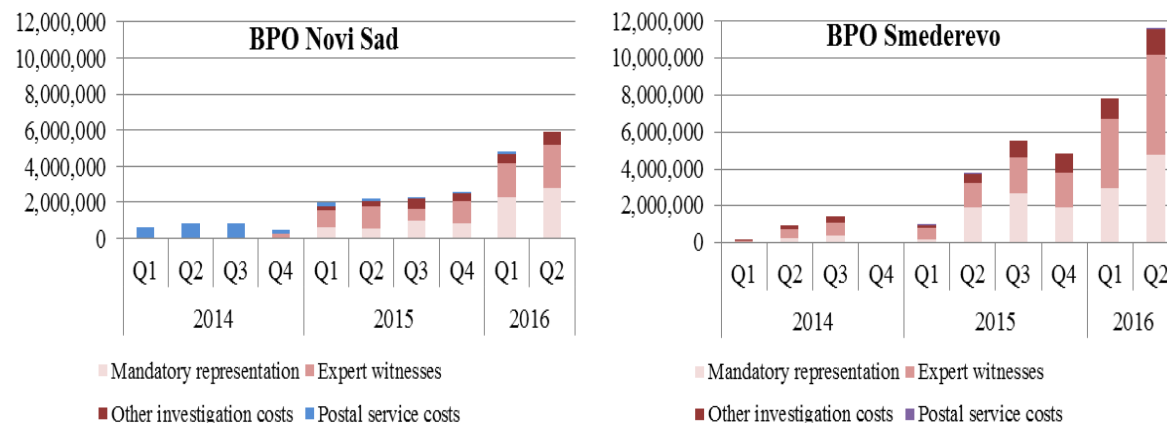
Table 5. Arrears per prosecutor in selected PPOs as of June 2016

PO	Number of prosecutors	Mandatory representation	Expert witnesses	Other investigation costs	Postal service costs
Beograd	43	417,058	176,837	3,094,221	0
Valjevo	4	391,875	764,602	82,403	0
Novi Sad	24	116,359	99,056	31,560	0
Prokuplje	3	3,424,189			25,784
Smederevo	6	792,436	904,740	233,229	9,113

source: POs quarterly arrears report

39. Trend in arrears accumulation is increasing rapidly in the first two quarters of 2016. Figure 6. below reveals trends in the level of arrears for BPPO Novi Sad and BPPO Smederevo. While it seems that arrears are accumulated evenly for all types of investigation expenditure, they more than doubled in first half of 2016 when compared to the figures observed at the end of 2015. They went from RSD 2.5 million to RSD 5.9 million in case of BPPO Novi Sad, while in case of BPPO Smederevo the increase was from RSD 4.8 million to RSD 11.6 million. When compared to the trend in commitments from Figure 4, we can see that patterns are similar with exception of the last quarter of 2014 when we assume there was a one-off allowance for settlement of arrears.

Figure 6. Quarterly arrears level and structure in BPPO Novi Sad and BPPO Smederevo



40. The list of largest creditors per PPO shown in Table 6 adds to the impression of prioritization and selectivity in payment execution which is imposed by the scarcity of funds available. This is supported by the structure of five largest creditors of HPPO Belgrade, HPPO Valjevo and HPPO Smederevo shown below. While HPPO Belgrade's and HPPO Valjevo's largest creditors are public institutions (mainly Forensics Institute and Military Medical Academy), those of BPPO Smederevo are mainly expert witnesses. Also it is interesting to note that the largest creditor of HPPO Valjevo is an expert witness with RSD 740,000 of accumulated arrears ¹⁴. Hence, while there is an evident lack of funds available, there does not seem to be a standardized approach in paying the bills and settling arrears, for that matter. Instead accounting departments are somewhat forced into prioritizing when making payments to ensure normal functioning of their offices.

¹⁴ This is the total amount due. Usual expert witness fees for individual cases range from RSD 10,000 to RSD 25,000. This can of course vary much depending on the complexity of their expertise and services rendered.

Table 6. Largest creditors as of November 2016

HPO Belgrade		
Number	Creditor	Amount
1	Forensic Institute	53,817,171
2	Military Medical Academy	30,279,822
3	Faculty of Biology	21,754,553
4	Lawyers	17,933,505
5	DNA tests	15,516,200
BPO Smederevo		
Number	Creditor	Amount
1	City of Smederevo (PUCs)	1,964,800
2	expert witness	1,738,172
3	expert witness	974,887
4	expert witness	834,344
5	Ministry of Interior	659,268
HPO Valjevo		
Number	Creditor	Amount
1	expert witness	739,211
2	City of Valjevo (PUCs)	638,378
3	Security Information Agency	614,400
4	Ministry of Interior	611,040
5	Faculty of Biology	472,951

source: internal database and author's calculation

41. In total there has been only RSD 3.4 million arrears settled through enforced collection in the observed period¹⁵ and all of the enforced collection was initiated by lawyers, while there was zero enforced collection from expert witnesses. BPPO Prokuplje sticks out with RSD 2.2 million, while HPPO Belgrade and HPPO Valjevo had RSD 860,000 and RSD 333,000 of bills settled through enforced collection. BPPO Novi Sad and BPPO Smederevo have not had any enforced collection so far.

42. Enforced collection could become a major issue in the future. Although data was not complete, the cost incurred by PPOs through enforced collection which exceeds the original debt is in the range of 25-30% of the original debt. Hypothetically, this means that if all creditors went immediately to collect their debts through enforced collection there would be an additional RSD 143 – 171 million of additional costs incurred on top of the RSD 572 million of original debt.

¹⁵ This number excludes RSD 4.3 million of compensation enforced by the prosecutors which were not re-elected in 2010.

5. Main findings

43. Expenditure levels are increasing every year and there is much variation in investigation related expenditure per case across the sample PPOs. Combination of the increasing new cases and large number of cases transferred from the courts in 2013 is causing current caseload to increase every year. However, the increase in expenditure is much higher than the rate of increase in the number of cases. Variation in the expenditure is striking – while HPPO Belgrade has on average 2.5 to 3 times higher expenses per case than HPPO Valjevo, in the BPPO category, BPPO Prokuplje is paying on average twice as much per case compared to BPPOs in Novi Sad and Smederevo.

44. Expenditure verification process is subject to interpretation and lacks clear guidance. The Rulebook on Charges in Judicial Proceedings is unclear and expert witnesses may arrive at amounts which can vary significantly. For instance, charges are based on the number of working hours which can be manipulated. Also charges may be doubled if services are rendered in “bad conditions (at night, at very bad weather conditions, etc.)”. This enables prosecutors to somewhat negotiate and rationalize as to whom and how much to pay which has adverse effect on their professional integrity and may have long –term implications on PPO performance.

45. Systems used for commitment control are inappropriate as they magnify the risk of arrear accumulation. The FMIS does not support encumbrance (i.e. reservation of appropriation) once commitments are entered in the system. PPOs do not use FMIS at all for recording commitments. Instead, they use their accounting software (ZUP) which is very rigid and does not allow effective data analysis. ZUP is also not integrated with FMIS. Most accurate evidence of commitments is, however, kept in notebooks of chief accountants and spreadsheets for easier data manipulation.

46. There are substantial differences in the process of commitment assumption among PPOs. This stems from different interpretation of the article 261 of the Criminal Procedure Code which is insufficiently clear as to whether the “award” of the lawyers and expert witnesses (which is the largest share of investigation expenditure) should be paid before the end of the investigation process or not. Also, the provisions of the article mention that expenses should be borne by the “institution managing the process” which some PPOs interpret as a possibility to transfer their expenditure to courts in cases when indictment is issued. This has caused PPOs that are three to four times larger both in terms of the number of prosecutors and their caseload to have comparable level of commitments as their smaller counterparts.

47. The unstandardized practice in commitment assumption creates large potential for corruption and threatens to jeopardize integrity of the PPOs. Although differences exist, the practice of each PPO can easily be modified to suit the current needs of a prosecutor or a PPO.

Invoices of expert witnesses with expertise which is scarce or particularly important for investigation are treated with priority. Current FMIS framework which does not support commitment control allows for this as commitments recording takes place in a parallel system which is not functionally linked with it. Payment orders are created directly in the FMIS with no reference to the order in which commitments are assumed.

48. Arrears reflect differences in commitment procedures and they are on average 2.3 times higher than the annual budget for investigation services . Those PPOs with more “loose” practice of commitment assumption and the possibility to transfer their costs to courts have expectedly lower level of arrears than those who immediately assume commitments once invoices of lawyers and expert witnesses come in. Settling all the investigation related arrears in one go, would require average annual budget for investigation to increase by 230%.

49. Enforced collection is currently relatively low but could represent a large issue in the future. Total amount of money that was collected by creditors through enforced collection was a modest RSD 3.4 million in the period from January 2014 until June 2016. At the same time, two out of five PPOs from the sample had zero enforced collection. Finally, when enforced collection procedure is applied, the expenses that go beyond original debt are around 25-30%. This means that if all creditors would reach out for it, additional RSD 143-171 million of costs would be incurred on top of the original debt of RSD 572 million (current level of arrears).

Recommendations

50. Better management of commitment control aligned with appropriate utilization of services provided which have been analyzed in this report is a prerequisite for improvement of financial management of SPC and PPOs. Based on the available information, the team is of the opinion that any budget increase earmarked for settling arrears, which could happen prior to significant improvements of the financial management function in the SPC and PPOs, will practically endorse current bad practice. In addition this would seriously undermine the integrity and performance of the public prosecution and judiciary in general.

51. The straightforward way to deal with the accumulated arrears is to simply settle them with higher budget appropriations in the coming years. However, the box bellow presents a list of recommendations which would be implemented before any budgetary increase is to take place. These interventions are designed to protect integrity and increase financial and overall performance of PPOs.

- **Recommendation 1:** Create a list of appropriated services, together with a range of acceptable costs per case, aimed to enhance transparency of budget planning and execution and prevent discrepancies in cost per case observed across PO network. This would be done by the SPC and RPPO with support of MoJ.
- **Recommendation 2:** Enhance the provisions of the Rulebook on Charges in Judicial Proceedings in order to exclude favoritism from cost setting. The prosecutors will have less problems to verify costs if a list of prices per different expertise which would be adjusted annually is introduced. This would be done by the SPC, RPPO.
- **Recommendation 3:** Ensure that commitments are recorded in ZUP and that these records are available to SPC in real time. In order to make this uniform provide training program for all accounting officers in PPOs on how to enter this information in the system. This would serve as an interim solution until full commitment control function is supported by the FMIS. This would be done by the SPC, RPPO and Judicial Academy.
- **Recommendation 4:** Establish standardized practice for assuming commitments by ensuring common interpretation of the article 261 of the Criminal Procedure Code. This would be done by the SPC and RPPO.
- **Recommendation 5:** Gradually increase budgets of PPOs to better reflect their needs as the above reforms are advancing in implementation. This has to be paired with regular monitoring and analysis of arrears. Based on this, the SPC will engage in dialogue with the MoF on how to eliminate arrears through appropriate budget planning.

ANNEX 1

Total arrears accumulated per BPPO, end of September 2016

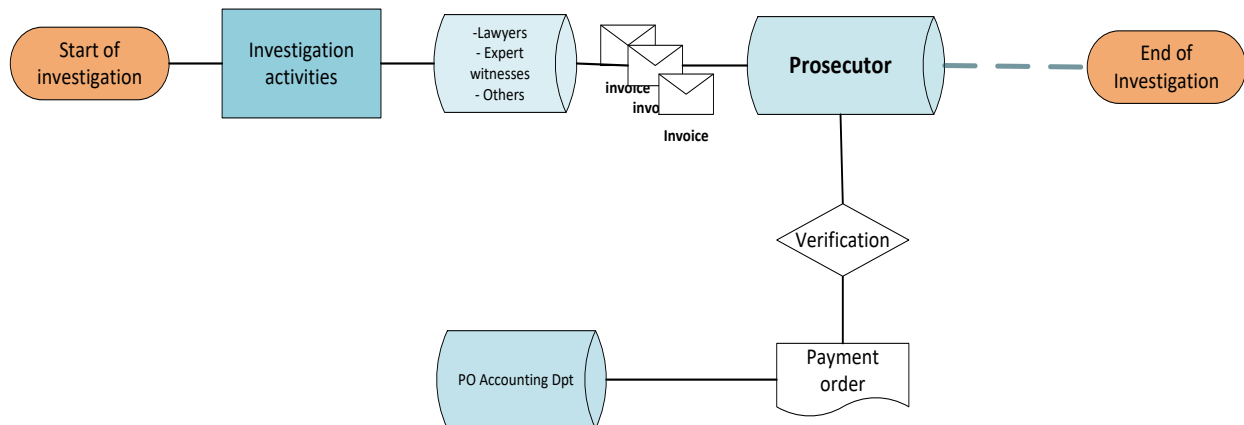
BPO	Arrears from before 201	Arrears from 2016	Total Arrears	Number of prosecuto	Arrears per prosecutor
Beograd 1	0	0	0	43	0
Beograd 2	0	0	0	25	0
Beograd 3	0	0	0	21	0
Kosovska Mitrovica	0	68,762	68,762	14	4,912
Despotovac	0	180,644	180,644	3	60,215
Lebane	0	205,047	205,047	1	205,047
Leskovac	0	2,228,383	2,228,383	9	247,598
Prijepolje	0	1,512,181	1,512,181	5	302,436
Negotin	127,716	1,420,340	1,548,056	5	309,611
Backa Palanka	0	633,481	633,481	2	316,741
Novi Sad	1,197,842	7,183,578	8,381,420	26	322,362
Cacak	0	3,465,081	3,465,081	10	346,508
Valjevo	0	4,622,156	4,622,156	11	420,196
Vrsac	30,756	3,215,659	3,246,415	7	463,774
Krusevac	0	3,416,766	3,416,766	7	488,109
Mionica	0	987,062	987,062	2	493,531
Vrbas	1,338,319	1,131,287	2,469,606	5	493,921
Novi Pazar	1,364,501	2,160,051	3,524,552	7	503,507
Kraljevo	0	5,226,116	5,226,116	10	522,612
Pozarevac	0	1,075,830	1,075,830	2	537,915
Gornji Milanovac	0	562,000	562,000	1	562,000
Uzice	0	3,451,844	3,451,844	6	575,307
Petrovac na Mlavi	0	576,372	576,372	1	576,372
Raska	0	585,022	585,022	1	585,022
Sabac	0	4,702,402	4,702,402	8	587,800
Veliko Gradiste	0	628,681	628,681	1	628,681
Pozega	577,030	2,231,091	2,808,121	4	702,030
Nis	0	13,574,320	13,574,320	19	714,438
Sombor	0	5,072,261	5,072,261	7	724,609
Becej	50,520	1,423,927	1,474,447	2	737,223

BPO	Arrears from before 2016	Arrears from 2016	Total Arrears	Number of prosecutors	Arrears per prosecutor
Loznica	0	5,260,000	5,260,000	7	751,429
Kursumlija	0	1,588,576	1,588,576	2	794,288
Trstenik	0	1,896,617	1,896,617	2	948,309
Sremska Mitrovica	230,500	6,581,072	6,811,572	7	973,082
Kragujevac	1,615,000	14,856,400	16,471,400	16	1,029,463
Arandjelovac	203,927	2,924,887	3,128,814	3	1,042,938
Bor	677,162	3,683,263	4,360,424	4	1,090,106
Mladenovac	1,707,134	3,831,754	5,538,888	5	1,107,778
Vladicin Han	167,656	3,288,456	3,456,112	3	1,152,037
Lazarevac	2,297,334	2,553,767	4,851,101	4	1,212,775
Vranje	2,999,670	9,363,707	12,363,377	10	1,236,338
Aleksinac	297,259	3,617,946	3,915,205	3	1,305,068
Obrenovac	2,333,836	4,410,168	6,744,004	5	1,348,801
Pirot	0	5,575,143	5,575,143	4	1,393,786
Jagodina	2,544,215	7,553,071	10,097,286	7	1,442,469
Pancevo	2,600,836	9,560,808	12,161,644	8	1,520,206
Stara Pazova	3,288,098	4,410,155	7,698,253	5	1,539,651
Subotica	139,780	12,183,304	12,323,084	8	1,540,386
Zajecar	24,910	12,341,804	12,366,714	8	1,545,839
Ub	532,925	2,661,159	3,194,084	2	1,597,042
Paracin	611,214	2,633,955	3,245,169	2	1,622,585
Kikinda	0	6,586,994	6,586,994	4	1,646,749
Velika Plana	1,236,882	5,444,388	6,681,270	4	1,670,318
Zrenjanin	593,112	7,764,694	8,357,806	5	1,671,561
Senta	1,968,000	5,311,646	7,279,646	3	2,426,549
Smederevo	2,832,535	14,308,021	17,140,556	7	2,448,651
Prokuplje	2,234,481	9,490,302	11,724,783	4	2,931,196
Ruma	937,429	8,014,780	8,952,209	3	2,984,070
Brus	0	644,607	644,607	0	0

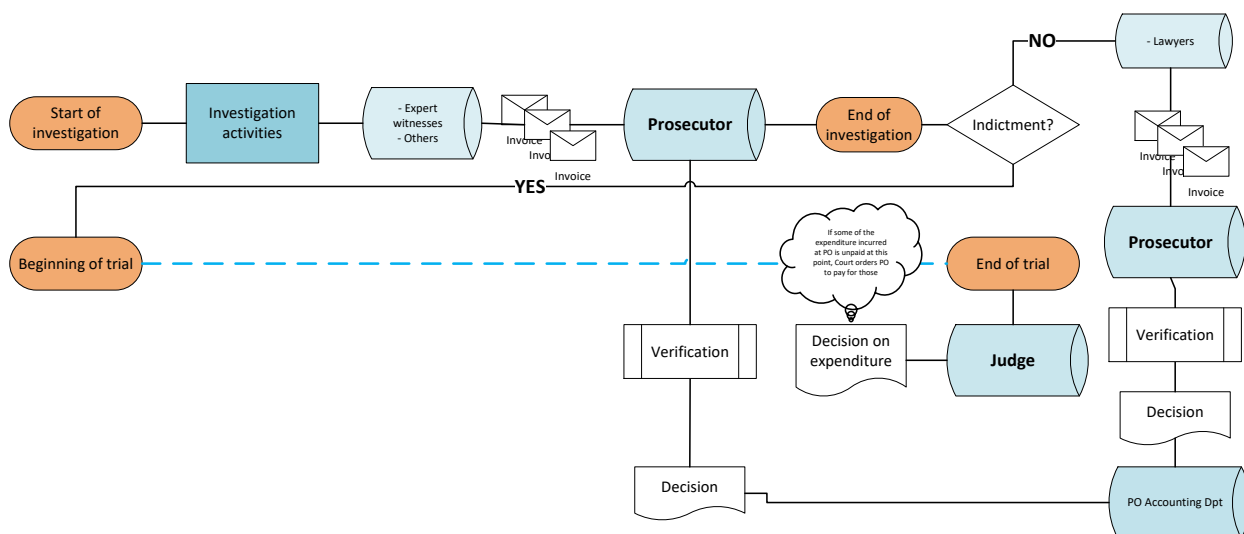
ANNEX 2

Process of assuming financial commitments in selected PPOs – process flowchart

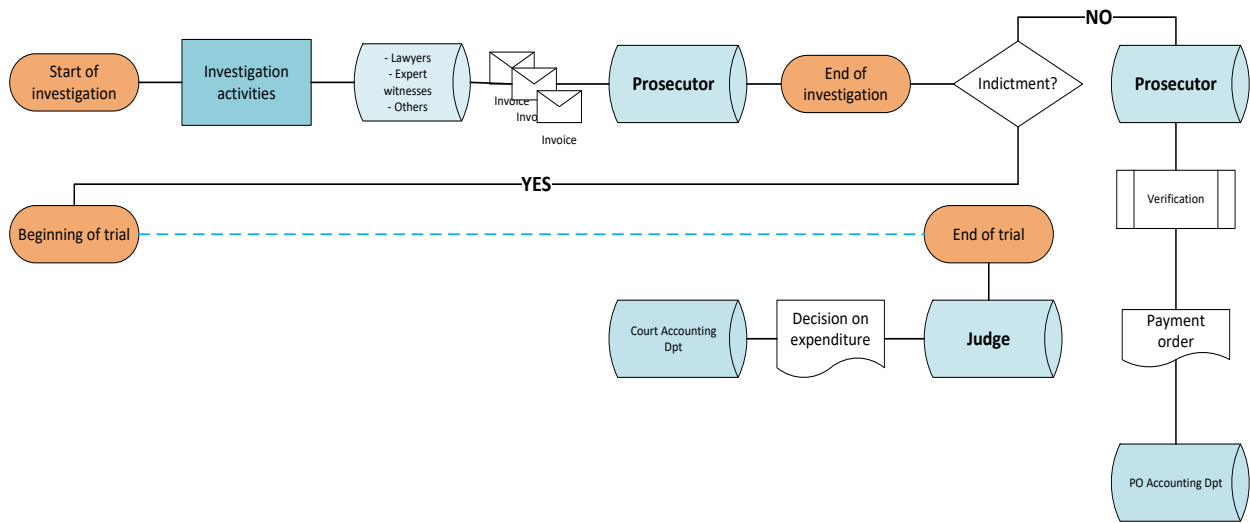
BPPO Smederevo



HPPO Belgrade



BPPO Novi Sad



ANNEX 3

List of interviewed people

1. Svetlana Nenadic, member of the State Prosecutorial Council
2. Tamara Smrkulj, Head of Financial Department of the SPC
3. Anela Grbovic, Senior Advisor at the Financial Department of the SPC
4. Natalija Vukasinovic, Head of the Financial Department of BPO Smederevo
5. Tanja Hinic, Head of the Financial Department of BPO Prokuplje
6. Jelena Boskovic, Public Prosecutor in BPO Prokuplje
7. Snezana Pavicic, Head of the Financial Department of BPO Novi Sad
8. Radivoj Kacanski, First Deputy Public Prosecutor in BPO Novi Sad
9. Zlata Ilic, Head of the Financial Department of HPO Valjevo
10. Mila Maksimovic, Deputy Public Prosecutor in HPO Valjevo
11. Sladjana Bogdanovic, Advisor in the Financial Department of HPO Belgrade
12. Svetlana Bogdanovic, General Secretary of HPO Belgrade