

20.10.2008

Port of Belgrade ownership concentration report

The Anti – Corruption Council deals with individual cases only if they indicate a wider phenomenon which especially emphasizes the sources of grand corruption in politics and economy. One of these cases is the concentration of the ownership which was executed in the Joint – Stock company Port of Belgrade in the end of 2005, which remained almost unnoticed in public, but we begin to feel its effects now, and we are going to feel them in the upcoming decades as well. This case is interesting because it has all the characteristics of so called secondary privatization – a process where the shares of the employees are transferred to the richest people in the country, who have good connections with politicians and state institutions. In a process of the secondary privatization, the foreign shell companies (companies without equity or revenues) are used in order to make an impression in public that those investments are actually foreign investments. Acquisition of shares, with a lot of breaches of law, is usually conducted with capital which origin is unknown, although it is usually the case that money traces lead to Cyprus and the assets which were transferred from the country during the nineties of the last century. After successful acquisition, the new owner usually becomes the monopolist and makes remarkable profit. If the plans for construction of new business and residential objects in the area of the actual Port of Belgrade and its surroundings were accomplished the new owner's profit could be measured in billions of euros. Consequently, this case is unique and arouses special attention.

Ownership concentration and monopolies

Ownership concentration is executed when a small number of shareholders get into possession of majority interest. Consequently, it can have significant positive effects when issuing business efficiency: the management of a company can be easier controlled by a small number of owners than a huge number of shareholders, especially when small shareholders are not completely informed about the nuances in business decision making. With strict control of the management, the owners are able to impose business decisions to a great extent, in order to enlarge the value of the company and of course, the value of their own investment. Higher company's value means that the company's resources are used in the best possible way, which makes conditions for income growth, employment growth and the implementation of new technologies. In a word, it appears a pattern where putting the individual interests in foreground can lead to the greatest welfare for the whole society. Such are the consequences of the ownership concentration in the rich economies where the stockholders equity (national capitalism) is widely spread. Similar effects can be noticed in those economies where markets are not so developed, but the rules are very clear and are completely obeyed. On the other hand, positive effects of the ownership concentration in our country are rare and moreover, it is common case that positive effects are overpowered by the negative ones. Ownership concentration in our country is carried out in specific conditions, without totally completed rules, or the current legislation is not fully applied in practice. It seems that two particular elements are especially emphasized here, and that is the crucial influence of political factor on economic issues and a fact that **the capital which was taken out from the country during nineties plays a dominant role on capital market.** These factors contribute to the creation of such ambient which is suitable for the grand corruption flourishing and even more, they create an inefficient economic system where so called big players, who have created a special political – economic monopoly have a prevailing role.

Namely, the big capital is interested in acquiring major interest in companies which already possess, or which can easily accomplish, the dominant position on the market. The easiest way for accomplishing that aim is, at first, providing ownership concentration in the corporation through political influence and thus providing a dominant position on the market. Every monopoly is economically inefficient, because it often offers goods with higher prices than concurrent bidders, it produces less, its expenses are higher and resources insufficiently employed. When a monopoly's position is protected by political support the negative consequences are long-lasting. It is possible that this rule would be confirmed unless the Government made resolute turn regarding its position towards market concentration and manipulations in a process of ownership enlarging in the companies with strategic importance. **Ownership concentration which has been carried out in the Port of Belgrade is an example of monopoly creation**

under protection of political factor and with an active participation of «runaway» capital.

Legislation

Law on Market of Securities (Official Gazette of SRJ no. 65/02 and Official Gazette of Republic of Serbia no. 57/03) regulated the takeover process of corporations during the time when the ownership concentration in Port of Belgrade was carried out. According to this law, share trading could be carried out only on the regulated market – stock market (Article 52) – and if a purchaser exceeded the limit of 25 % it would be obliged to request for a purchase approval from the Republic Of Serbia Securities Commission (Article 69). This way of share acquiring is called the takeover proposal and it was specially regulated (later on, the Law, which laid down the takeover issue, has been passed). The purpose of provisions is to disable possible abuses either on the side of supply or on the side of demand. According to the Law on Market of Securities the Commission has been empowered to regulate the entire process. In connection with this, the Commission specifies the contents of a bid which must be filled out in a special form by a purchaser and sent to all shareholders. The contents and form of the takeover bid proposal are specified in the Code of rules (Official Gazette RS no. 102/2003, 25/2004, 103/2004, 123/2004), which was adopted by the Republic Of Serbia Securities Commission. The Code has been amended several times, but at the time when the takeover bid for the Port of Belgrade was submitted, Article 7 specified all necessary documentation which should be attached with a request by a potential purchaser. The integral part of the Code are the Guidelines which bring more detailed definition of what the takeover bid should consist of. Item 4 of the Guidelines emphasizes that the data of the targeted Joint Stock Company (whose shares are about to be purchased) have to be given e. g. the value of property and capital, as well as other relevant data regarding the Joint Stock Company should be well known to a bidder. Item 5 defines data regarding bidder, inter alia the value of its core capital (for a company, not for an individual), data about individuals who have more than 1/10 votes in the Assembly of a bidder, data regarding statement of assets and liabilities and profit and loss account etc. If all data were available and if those data were in accordance with other notified documentation the Commission would approve the takeover bid (Article 8 of the Code). Board of Directors of a Joint Stock Company has the most reliable information regarding the affairs of a company business. The Law, in Article 72, foresees that the Board of Directors can, within a period of 10 days from the day of the takeover bid submission, notify shareholders about a bid and instruct them on decision making (whether to accept the bid or not). In its notification the Board is obliged to disclose all information about important changes which have occurred from the day of conducting the last financial report, in other words, annual report (Item 8 of the Guidelines about contents and form of the Board notification referring to the share takeover bid).

Concentration

in

practice

Port of Belgrade covers the area of about 220 hectares of land in the central city area between Francuska street and Pančevo Bridge (municipalities Stari grad and Palilula). Master plan of Belgrade until 2021 (Official Gazette of city of Belgrade no. 27/03), in Item 4.4.9 foresees that Port of Belgrade should remain the business area, which is also planned to be widened. Only three years after the Belgrade Master plan has been issued, which defines the purpose of the land until 2021, the Belgrade Land Development Public Agency, on 27. December 2006, notified Public invitation for conducting the preliminary advisability study with a master project for a new mechanized cargo port in Belgrade. Public invitation came after the share takeover of the Port of Belgrade in September 2005. Apparently, the change of the purpose of the land and the port relocation had been previously agreed, and the Belgrade Land Development Public Agency was supposed to conduct and justify that agreement by ordering the advisability study. Although the Master plan has not been changed and no decision on purpose of the land modification and relocation of the port has been issued, the acting Mayor of Belgrade Mr. Zoran Alimpić presented the new port project in November 2007. On that occasion he told that «Master plan until 2021 and Master plan of inland waterways of Serbia until 2025 foresee the construction of a new cargo port on the Danube. The location on the right bank of the Danube, from Dorćol to Ada Huja of 480 hectares, where the port is currently located, is to become the area for construction of business-residential buildings». (Glas Javnosti 6. 11. 2007).

The actual port is located on the potentially most attractive spot in the core down town, because the building of the business-residential complex is also planned on the nearby, downstream land on the area of 500 hectares. Regarding this matter, it is obvious that both the land of the port and the downstream land have the great value. Port of Belgrade company, which uses above mentioned 220 hectares, was privatized in 1998 according to the at the time existed Law on Ownership Transformation, when the 60% of the shareholders capital was divided to the employees for free, 30% was transferred to the Share Fund and 10% to the Pension Insurance Fund. The assessment of capital value was carried out with the current account from 31.12.1998. As the assessment was significantly below the market value, the management of the company decided to conduct a new assessment of

the capital value in 2005. Regarding this issue, the Institute of Economic Sciences was commissioned in the April of the same year. The Institute submitted the preliminary results to the company in June 2005, when stated that there were some important differences (over 3.5 times higher) between the accounting value and capital value which was obtained by implementing the international accounting standards. In the same month the management of the company informed the Ministry of Justice, Share Fund, Privatization Agency and the Securities Commission that there was a modification regarding assets value which caused the change regarding capital value and that it was in the best interest of shareholders including the state, as the individually biggest holder, to wait with the selling of the shares.

However, although the Institute did not finish its work, i.e. the capital value in the balances of the company has not been modified, the Board whose members were professor Dr Vladeta Čolić, the president, Vladeta Blagojević, professor Dr Mirko Vasiljević, Miroslava Drobac, Dušan Kosovac, as members, scheduled the Annual Shareholders Meeting for the 9. of September 2005. On that meeting, financial reports were discussed and the business policy was adopted. On that occasion, the management informed shareholders about the contract which had been signed with the Institute, but the financial reports were adopted without previous adjustment of the capital value. Supervisory Board (Professor Dr Danijel Cvetičanin, the president) also omitted to warn the Assembly on that fact, so the shareholders stayed in delusion that the value per share was 494 din. The day the meeting was held on September 9, 2005. The Securities Commission approved the bid of the **Worldfin Company from Luxemburg for takeover of the Port of Belgrade**. The bid was issued through the BDD M&V Investments from Novi Sad (the same firm had participated in purchase of C Market shares). The text of the bid was published in the next day daily newspapers. The offer was opened until September 30, and according to it the share price amounted 800 din. The Board of Directors informed the shareholders by an advertisement on September 21. It cited that the assessment of the capital (property) value of the Port of Belgrade was in process and since the actual value was higher then the accounting one, the Board recommended the shareholders to wait until September 23 «and that they should, after the deadline has expired, depending on whether there are some other competing bids or not, decide to deposit shares, in order to sell them, or not.» Until September 23, not one competitive bid had occurred and the shareholders disposed their shares. The Institute submitted its findings on September 27, and based on them the share price was 1774 din. The very same day The Privatization Agency decided that the takeover bid was accepted and it issued an instruction to the Share Fund to sell all the shares in possession (40,88% shares). The takeover bid was successful and Worldfin acquired more then 93% of Port of Belgrade shares. Share price which was paid amounted 800 din. Worldfin company from Luxemburg, which purchased the shares, was registered in Rue d'Arlon 207, just as the Novafin company which acquired C Market shares only a few days after it was founded. In its takeover bid the **Worldfin stated that it is a new company, so there were not any balances or financial reports**. According to the Court Registrar registration certificate, core capital value of this company was 31.000 EUR. The company does not have a share in the core capital of other legal entities.

Unanswered

Questions

The first thing is, how is it possible that a company which core capital amounts 31.000EUR and which does not have any connection with other legal entities can pay almost 40 million EUR for Port of Belgrade shares. Almost in the same period (the end of 2005) the same pattern was used when the small C – market shareholders' shares were purchased – the shares were purchased by a company without any turnover or property, except the minimum start-up capital and the amount was 44 million EUR. It is more then clear in both cases that the shares were purchased for another purchaser who stayed in the shade. **How did the Securities Commission overlook these facts and why The Administration for the Prevention of Money Laundering did not react?**

Why did the Commission approve the takeover bid in spite of some contradictory statements? Namely, the bidder emphasizes that «it does not have any information about assessment of capital or assets» and that «there are not» any other important data regarding Joint – Stock Company that are well known to the offeror. On the other hand, the offeror states that there were some contacts with the management of the company. It is not realistic to think that the people from the management while contacting potential purchaser avoided to mention that the accounting value was to low and that the revaluation proceeding was in process. In other words, if they did avoid that, they were acting in the purchaser's favor and not in favor of its own shareholders and according to it, the Commission was obliged to react. The Commission was also informed on capital revaluation, so it could inform the offeror on that matter. So, it is clear that the purchaser had key information and it did not want to include it into the takeover bid.

Another information which can be noticed is that the Worlfin company was registered on the same address as the

Novafin company which acquired the retail store chain C – market. According to the testimony of Mr. Milan Beko before the Special Department of the Belgrade District Court in the proceedings against Mr. Slobodan Radulović it is obvious that it is not just a pure coincidence. The witness stated that the Novafin Company «was established for that purpose» and that it is a common thing in that kind of business to establish «companies for special purpose without direct connection with their names - they are taken out from the drawer». On that occasion the witness also stated that he runs number of companies, he called them “shell companies”, which do not have any turnover. They have been founded for accomplishing of a concrete task. Novafin`s task was purchasing of C – market`s shares and Worfin`s task obviously was purchasing of the shares of Port of Belgrade. How is it possible that none of the state institutions have reacted on the public confession regarding the role of the shell companies?

In both cases the price which was paid to the shareholders was significantly lower then the actual one, but moreover, the fact that concerns the most is that it was done in favor of the owners who had remained undeclared. Regarding C – market issue The Commission for Protection of Competition has ascertained that the Hemslade Trading company from Cyprus, which is the owner of Delta Holding, has purchased the shares of C – market which led to the monopoly position of that company in grocery retailing. In the Port of Belgrade case the actual owner has not been officially established yet, but however, regarding the above mentioned, the assumption that it is the same owner is pretty convincing. In the first case the majority shareholder had a monopoly position in retail trading, and in the second case the major part of the free urban building land in the central area of Belgrade.

The question remains, why no one of the state institutions or officials (either on state or local level) has mentioned the establishing of the monopoly which exceeds the frames of a particular economic branch? How can we explain the synchronized acting of state institutions, shares` purchaser and the management of the company during the purchasing process (ownership concentration) in the Port of Belgrade? It can be easily noticed from the dates and contents of the particular events:

- The Board was officially informed, latest in June, that the actual property value of the company was much higher then accounting one. Because of that, state institutions were informed on this matter. However, the Board scheduled a shareholders meeting before receiving the final value assessment and state institutions did not react.
- On the day of the shareholders meeting the Securities Commission approved the takeover bid ignoring the major difference between the accounting and the actual capital value.
- In the takeover bid, it is stated that the representatives of purchaser have had a conversation with the management of the company about the possibilities of purchasing shares of the company and they sent an investment letter of intent. The Assembly of shareholders was not informed about these issues. The Board did inform shareholders by an advertisement that the offered purchasing price was too low, but it also recommended that shareholders should decide on the issue depending on whether there were some other competitive offers until September 23 (the closing of the offer was on September 30, although the Worldfin accepted an obligation for purchasing the shares, under the offered price, for 20 more days from that date).
- Privatization Agency issued an order to the Share Fund to sell the shares of the Port of Belgrade the very same day when the final value assessment was issued, although it received information that the bookkeeping capital value of the company was unreal, three months earlier. That way the State has lost at least 21million EUR which is an amount of the difference between the estimated value of the purchased shares and the price which was paid.

- The State decision to accept the offer three days before the closing sent a direct message to the small shareholders that they should also accept the offered price. Maybe it is not worthless to mention a fact that the official representative of the Worldfin in the takeover process of the Port of Belgrade was Mr. Vuk Delibašić (the director of Primer C, appointed by Novafin company, the company which temporarily took over the shares of C – market) the person that was employed in the Privatization Agency until the end of 2002. Also, the Executive Director of the Agency Mr. Goran Mrđa who was in position until the end of 2005 is currently member of the Board of the Port of Belgrade. Finally, one can ask a question why the Belgrade citizens are forced to build a new port on the Danube in order to give away the most attractive urban building land to the company without equity or revenues.

Recommendations to the Government

The liability of the participants in this process should be examined by the authorized state institutions. It is Government`s responsibility to recognize all system`s consequences of this and similar cases. At the very beginning of this report it was pointed out that the ownership concentration in market economy is often very prosperous because it increases the owner`s (principal) extent of control over the management of the company (agent). There is no doubt that the similar effects could be expected in our economy if we could

eliminate the negative conditions regarding concentration process. However, one must bear in mind – macroeconomic consequence of the ownership concentration, which cannot be fully expressed in the developed economy.

Ownership concentration significantly reduces the number of shareholders in our country. It also reduces the credibility of the capital market and readiness of people to invest in shares. For example, with the concentration in companies C – market and Port of Belgrade the number of shareholders of these companies decreased from 9624 to 1058, where every one of the small shareholders (individually or collectively) is disabled to influence the company's business policy – in both cases, only one owner makes all key decisions.

In situation like this in our country, where the corporate managing is underdeveloped i.e. where small shareholders' interests are not respected, the most important thing in practice is to provide over 50% majority at the Shareholder Assembly in order to accomplish a full control over the company and to impose the major owner's will.

The consequences are multiple: potential investors are not interested to invest into companies where they can not have major ownership, the price of minority shares remains permanently low and the capital market cannot escape from the vicious circle of underdevelopment. Simply, people are not confident regarding investing in minority shares and on the other hand, the major owner is not interested in purchasing minority shares because it controls the company without those shares. Accordingly, the stock market transactions of such companies are insignificant and they just formally exist on the stock market listing. Without fully developed capital market, the offer and demand of available financial property must be carried out only through the banking sector. As the competition in this sector here is still not the rule, and agreement is an exception, but vice versa – the competition is an exception – the interest rate must be high, so it is rare to find some profitable projects. All these facts lead to decrease of economic development and to the high unemployment rate on long-term basis as well.

The Government has to be aware of all these macroeconomic consequences of its acting, in other words non acting. Regarding this particular case, it has to take into consideration the fact that the ownership concentrations, like in Port of Belgrade, C – market, Knjaz Miloš, and in many other companies as well, create prerequisites for permanent nonfunctioning of the capital market. On the other hand, the way of dealing these concentrations, accompanied with a number of frauds, with acting of state institutions in favor of the big capital, with bending the law by overlooking indisputable facts or regulations, contributes to the growth of the instability of property rights. In our country, small shareholders cannot be sure that their legal rights will be obeyed – the dividends are not paid, even if the company makes profit, and the profit is often unexpressed through “creative bookkeeping”. The only option for the shareholders to sell their shares is the stock market, but even there, they are faced with the underestimated value of their shares. Accordingly, it is not weird that the small shareholders strive to get rid of their property rights. The acting of the state institutions, first of all the Privatization Agency and the Share Fund, only strengthens the insecurity of property rights, which can easily be seen in this particular case. Without the security of property rights there is no development of market economy and finally of the democratic political system as well.

The Government has to be aware of all political consequences of the ownership concentrations like it was done in the Port of Belgrade and C – market. Both ownership concentrations were carried out through firms that were registered abroad in order to participate in the privatization process. The capital they use is of unknown origin, although in one particular case it was realized that it came from Cyprus. That capital is managed by the people who were highly ranked in the Milošević's regime (Miroslav Mišković and Milan Beko). This fact should not be underestimated and the Government's task is to investigate (together with Cyprus authorities) what was the amount of the capital outflow during nineties, which are the channels of the capital current and to identify the cases where it was legalized in the privatization process. This should be carried out in cooperation with specialized international institutions referring to the provisions of the UN Convention against Corruption (Articles 46 and 48). This is not just a necessity, but also an obligation for the Government since our country, besides the UN Convention, has ratified the Council of Europe conventions against corruption.

The participants of above mentioned concentrations are among the richest people in this country and they strive to enlarge their wealth by creating monopolies. By purchasing the C – market shares they have created the retail sector monopoly and the first step in monopoly of residential building at the most attractive locations in Belgrade was done by purchasing the shares of the Port of Belgrade.

This report shows, like the report on C – market, that it is impossible to create a monopoly without support of the state. Thus, the potential monopolists are naturally interested in securing the state support for their activities and that is one of permanent resources of grand corruption. On the other hand, creating a monopoly causes the

permanent source of the economic inefficiency – monopoly charges customers higher price, pays lower price to the suppliers and anyway, it engages less capital and labor than in the case where the competition existed. Accordingly, the direct task of the Government is to improve the competition on the market and to support the acting of Regulatory Bodies, first of all the Commission for Protection of Competition.

One of the basic constants of all democratic governments from 2000 was support to the privatization process without the questioning the sources of capital. Such approach led to the legalization of illegally acquired wealth, but also to the great split within society. Serbia has become a country of poor citizens and extremely wealthy individuals. This situation contributes to the growth of grand corruption, first of all by the non transparent financing of the political parties. However, the consequence of that fact, which is maybe more important, is that the extreme polarization regarding wealth cannot be suitable for strengthening of the democratic political system. The extreme gaps in wealth lead to the extreme political positions and they do not contribute to the strengthening of democratic values in a society.

Belgrade, February 19, 2008

PRESIDENT
Verica Barać

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