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# **Federal Republic of Yugoslavia**

## **Country Strategy Paper**

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## Introduction

As provided for in the CARDS regulation<sup>1</sup>, the Country Strategy Paper (CSP) provides a strategic framework through which European Community (EC) assistance will be provided in the period 2000-2006.

The CSP for the Federal Republic of Yugoslavia (FRY) sets out the EU's co-operation objectives, policy response and priority areas for co-operation based on an assessment of the FRY's policy agenda and its political and socio-economic situation. The multi-annual indicative programme (MIP) annexed to the strategy sets out the EC's response in more detail, highlighting programme objectives, expected results and conditionality in the priority areas of co-operation for the period 2002-2004. The indicative financial allocation for CARDS support to the MIP is €960 million under the National Programme with an additional €31 million from the CARDS Regional Programme.

The Federal Republic of Yugoslavia (FRY) is made up of the Republic of Serbia and the Republic of Montenegro. The Republic of Serbia, in turn, includes the provinces of Vojvodina and Kosovo. While taking account of the sovereignty and territorial integrity of the FRY, the UN has placed Kosovo under an interim international civil and military administration, following the 1999 conflict.

The FRY is situated in the Western Balkans and shares international borders with Hungary, Romania, Bulgaria, FYROM, Albania, Bosnia-Herzegovina and Croatia, and is thus a country of high geo-strategic importance for the stability of the whole region. Its sole access to the Adriatic sea is along the coast of the Republic of Montenegro.

The FRY covers a land area of 102,000km<sup>2</sup> and has an estimated population of 10.6 million (of which 650,000 live in Montenegro and around 2million in Kosovo). Some two-thirds of the population are ethnic Serbs but minority groups are also present. Ethnic Albanians account for 12% of the overall population and other distinctive groups include Hungarians, Bosniacs, Romanians and Roma. There are some 384,000 refugees in Serbia, plus some 14,500 in Montenegro - mostly coming from BiH and Croatia. As a result of the Kosovo conflict, there is also a large number - estimated at around 230,000 - of displaced persons (of whom around 90% are Serbs) who are now accommodated mainly in central and southern Serbia and Montenegro.

This strategy reflects the political and legal reality that the overall relationship of the European Union is with the Federal Republic of Yugoslavia while also taking account - but not prejudging the outcome - of two other ongoing processes:

- The efforts of the two constituent republics of Serbia and Montenegro to clarify their relationship within the Federation.
- The future status of Kosovo and its relationship with the Republic of Serbia and the FRY overall.

The CSP has been written to take this evolving situation into account. It sets out an approach that respects international and Community law, is consistent with EU policy and is relevant to all entities at the present time but also is designed to require the least modification possible, whatever the outcome of the above-mentioned processes.

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<sup>1</sup> Council Regulation (EC) No 2666/2000, OJ L 306, 7.12.2000, p.1

## 1 EU / FEDERAL REPUBLIC OF YUGOSLAVIA COOPERATION OBJECTIVES

### 1.1 CARDS

The EU's co-operation objectives with the FRY are anchored in the **Stabilisation and Association Process (SAP)**, a proximity policy which reflects the political and strategic importance of the Balkans to the EU. The Stabilisation and Association process is a framework in which a new contractual relationship (Stabilisation and Association Agreements) and an assistance programme (CARDS) help each country to progress, at its own pace towards EU membership.

The European Commission set out this ambitious vision for the region's development in a communication of May 1999. The approach is based on:

- (1) a recognition that one of the main motivators for reforms relating to respect for the rule of law, democratic and stable institutions, and the development of a market economy is a relationship with the EU that is based on a credible prospect of membership once the relevant conditions have been met;
- (2) the need for the countries of the region to develop bilateral relationships between themselves as a basis for greater economic and political stability in the region;
- (3) the need for assistance programmes and contractual relations, although anchored to a common set of political and economic conditions, to be flexible enough to allow each country to move ahead at its own pace to accommodate a range of situations, from post-conflict reconstruction and stabilisation to technical help with matters such as the approximation of legislation to the core elements of the *acquis*.

Following the Feira Council of June 2000, which confirmed that the EU's goal is the fullest possible integration of these countries into the economic and political mainstream of Europe, the Zagreb Summit of 24th November 2000 set the seal on the SAP by gaining the region's agreement to a clear set of objectives and conditions. In return for the EU's offer of a prospect of accession on the basis of the Treaty on European Union (TEU) and the 1993 Copenhagen criteria, and an assistance programme to support that ambition, the countries of the region undertook to abide by the EU's conditionality and participate fully in the Stabilisation and Association Process.

They also accepted that the Stabilisation and Association Agreements (SAAs), when signed, would be the principal means to begin to prepare themselves for the demands that the perspective of accession to the EU naturally entail. The SAAs focus on respect for democratic principles and integration of the countries of the region into the EU single market. They foresee the establishment of a free trade area with the EU and set out rights and obligations in areas such as competition and state aid rules, intellectual property and establishment, which will allow the economies of the region to begin to integrate with the EU's. The conclusion of such Agreements represents the signatories' commitment to complete over a transition period a formal association with the EU, tailored to the circumstances of each country but based on the implementation of the same core obligations.

The EU's political strategy towards the region relies on a realistic expectation that the contract it enters into with individual countries will be fulfilled satisfactorily. Careful preparation with each country before the EU offers such a contract has been and remains a vital component of the Stabilisation and Association Process. The agreements contribute to the EU's objectives in the following way:

- (1) They are a tool which provides, much as the Europe Agreements did for the candidate countries in Central Europe, the formal mechanisms and agreed benchmarks which

allow the EU to work with each country to bring them closer to the standards which apply in the EU.

- (2) They are a means to focus attention on respect for key democratic principles – human and minority rights, stable democratic institutions, standards of political behaviour and the independence of the media.
- (3) They include the core elements which are at the heart of the single market. Through free trade with the EU and the associated disciplines (competition and state aid rules, intellectual property etc) and rights (e.g. establishment), this process will allow the economies of the region to begin to integrate with the EU's.

Effective implementation of the Stabilisation and Association Agreements is a prerequisite for any further assessment by the EU of a country's prospects of accession. Each country will need time, help and encouragement to implement such obligations properly.

The SAp is not simply a bilateral process with each country: the Zagreb summit placed considerable emphasis on the need for regional co-operation. Similarly, the SAAs include a clear commitment to regional co-operation, which is reflected both by the funding of a regional CARDS programme and by the shared objectives of national CARDS programmes.

The CARDS programme underpins the objectives and mechanisms of the Stabilisation and Association Process, and as each country moves deeper into that process assistance will focus increasingly on support for the reforms and institution building necessary to implement the obligations in the Stabilisation and Association Agreements. A precondition for receiving assistance under CARDS is compliance with Article 5 of the CARDS Regulation (Council Regulation 2666/2000 of 5 December 2000) covering conditionality issues.

The indicative financial allocation for CARDS assistance for FRY for the period 2002-2004 is €960 million under the national programme, and a share under the CARDS regional programme for measures which will be implemented at Federal level, Republican level and in Kosovo. FRY will, in addition, benefit from up to €31 million under the CARDS regional programme for integrated border management.

## **1.2 The Federal Republic of Yugoslavia in the Stabilisation and Association Process**

The ultimate objective of EU political and economic relations with the FRY is to ensure that the latter makes the full transition to an open market economy and a democratic civil society through bringing its policies and legislation closer to those of the European Union, with integration and EU membership as the ultimate goal.

With the advent of democratic leadership, the FRY can now benefit *fully* from all aspects of the SAp according to the same conditions as the other participants, namely respect of democratic principles, human rights and the rule of law, undertaking market economy reforms, ensuring good-neighbourly relations and implementing obligations including those established by Dayton and UN Security Council Resolution 1244 (UNSCR 1244).

The FRY has not yet reached the stage of negotiating a Stabilisation and Association Agreement. However, a joint EU–FRY Consultative Task Force (CTF), involving representatives from Federal, Serbian and Montenegrin administrations and UNMIK has been established to support and monitor FRY's progress towards this stage. The first meeting of this CTF was held on 23<sup>rd</sup> July 2001 and the second on 6 November 2001.

The goal of FRY integration into European structures enjoys the explicit support of the wider international community. For the process of integration to be successful it is essential that the authorities in Belgrade, Podgorica and Pristina work closely to ensure that all parts of the FRY co-operate in meeting the requirements of the SAp.

### 1.3 CARDS Assistance

The main objective of CARDS assistance to FRY is to help pave the way to achieve the objectives described above – namely, the full participation of the Federal Republic of Yugoslavia in the SAp.

The CARDS Regulation foresees assistance for, inter alia:

- reconstruction, aid to refugees and displaced persons, and stabilisation of the region.
- sustainable economic development and market economy orientated reforms;
- the creation of an institutional and legislative framework to underpin democracy, the rule of law and human and minority rights, reconciliation, and the consolidation of civil society, the independence of the media and the strengthening of the rule of law and of measures to combat organised crime.
- social development;
- fostering regional, Trans-national, cross border and interregional co-operation

Though the EC's formal relations remain with the state<sup>2</sup>, the actual delivery of CARDS assistance is implemented at three different levels, depending on the nature of the assistance: through the federal authorities, through the authorities of the Republic of Serbia, Kosovo (under UN interim administration) and the Republic of Montenegro or directly to beneficiaries at grassroots level.

Further details on the scope of CARDS assistance for FRY are contained in the annexed Multi-annual Indicative Programme (MIP) 2002-2004.

## 2 THE FEDERAL REPUBLIC OF YUGOSLAVIA'S POLICY AGENDA

The overwhelming policy priority is the fundamental reform and restructuring of the federation which is the key to the survival of the FRY as a federal state.

The political and subsequent institutional arrangements currently in force are not functioning effectively. Various reforms which increased de facto responsibilities of the Montenegrin authorities have adversely affected the effectiveness of the Federation. Until the future status of Kosovo is resolved, local authorities and the international community will continue to face a challenge in the development of this Province. The lack of a functioning single economic space raises concerns for economic growth. For these reasons, one also needs to look to the Republican and Kosovo levels when examining the overall policy agenda of the FRY.

The *Republic of Serbia's* policy agenda is dominated by completing reconstruction and deepening economic reform and, on the political side, continuing the democratic dialogue with Montenegro, consolidating the solution following the earlier crisis in southern Serbia, resolving the status of Kosovo and enhancing diplomatic and economic relations with neighbouring countries. This will be complemented by the substantial strengthening of local government, the establishment of open, transparent and efficient public administration and state institutions and the reform of the judiciary with particular focus on tackling corruption and organised crime.

For UNMiK, responsible for the international civil administration of the province of *Kosovo*, the policy agenda is continuing implementation of UNSCR 1244, including the creation of the

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<sup>2</sup> Federal Republic of Yugoslavia - Framework Agreement, 25 November 2001.

provisional institutions of self-government<sup>3</sup> after the November 2001 elections and the development of a working relationship with Belgrade, as well as the consolidation of reconstruction and economic reform.

In the *Republic of Montenegro*, the policy priority is to define a new relationship with Belgrade, and to continue and deepen the economic and political reform process particularly through tackling issues of legislative reform and corruption which threaten the Government's ability to promote prosperity and provide effective services for its people .

The overall agenda for socio-economic and institutional reform in the FRY is largely in line with the recommendations of the Economic Recovery and Transition Program (ERTP) for the FRY as presented at the EC/World Bank Donors Conference on 29 June 2001 in Brussels and has been set out by the FRY authorities in the documents presented by them in the Conference. The macro-economic policy framework is set in the IMF Standby Programme that was approved in mid 2001 and successfully reviewed in September 2001.

## **2.1 Good governance and Institution building**

*Public Administration Reform:* The basic policies for public administration reform and strengthening the capacities of national institutions in the FRY are now in progress.

In 2001, *Serbia* announced the creation of a high-level Public Administration Council which will propose measures to increase the efficiency of Government, prepare with ministries a medium-term strategy for reforming public administration and monitor that strategy's progression. An Agency for Public Administration Development was also established by the *Serbian* government to act as implementing mechanism for reforms.

The Serb authorities also announced the establishment of a Public Administration Institute to undertake the long term training of civil servants. *Montenegro* has established a Public Administration Institute under the Ministry of Justice designed to carry out similar tasks.

UNMIK has enacted Regulation 2001/19 in *Kosovo*, establishing the executive branch of the provisional institutions. The priority is assisting capacity building of the public service and general institutional reinforcement.

Another of the main challenges recognised by the FRY is to combat corruption at all levels and this will be tackled in parallel with efforts to decentralise authority to the municipalities.

*Justice and Home Affairs:* Reform and strengthening of the judiciary and the police are considered by the authorities as key elements to enforce the rule of law, to reinforce democracy and to fight against corruption and criminality. FRY policy in this area is starting to be developed as shown by its increased cooperation with ICTY. In *Serbia*, a new draft law on the police is being discussed in 2001 and a multi-ethnic approach is now being taken on policing in Presevo. Similar efforts are being undertaken by UNMIK with greater implementation difficulty.

Organised crime remains a source of socio-economic and socio-political instability and concern for the FRY and tackling this is high on its agenda.

*Customs and taxation:* The three entities intends to give particular attention to the modernisation of customs and taxation, including anti-corruption measures. This reflects the high priority given to improving the collection of revenues, ensuring a level playing field for economic development and protecting social and economic interests.

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<sup>3</sup> UNMIK Regulation No. 9/2001 of 15 May 2001 on "A Constitutional Framework for provisional self-government in Kosovo "

## 2.2 Economic policy

*Fiscal Policy:* Against a backdrop of an shrinking economy, the FRY's entities have started radical economic reform although they are at different stages and are progressing at different speeds.

In 1998, *Montenegro* embarked on an initial economic reform and stabilisation programme with financial support of international donors and gradually obtained de facto autonomy over monetary policy, trade policy and customs. The Montenegrin government started a public finance reform programme in late 2000, aimed at increasing fiscal transparency and improving budgetary procedures, revenue collection and expenditure control. These important reform steps were facilitated by conditionality requirements attached to donor contributions.

In *Serbia*, the stabilisation and reform programme of the new democratically elected authorities led to a strong tightening of revenue collection and budget expenditure. Improvements to public expenditure management are starting, with a number of laws in 2001 creating the basis for enhanced budgetary planning and control. Lastly, a comprehensive tax reform was passed through the Serb Parliament with a view to lowering the number of taxes and tax rates, broadening the tax base and reducing the previous practice of ad-hoc exemptions.

As for *Kosovo*, UNMiK established the Central Fiscal Authority (CFA) in 1999, with specific responsibilities for design and execution of the Kosovo budget, a tax administration and a customs service (supported by the EC funded Customs Assistance Mission in Kosovo CAM-K). Impressive progress has been achieved to build up a domestic revenue base and the 2001 budget has increased the share of expenditure covered by domestically generated revenues from about half to over two thirds. UNMIK's medium-term fiscal strategy acknowledges the necessity to make progress towards a self-financed budget, to increase budget sustainability and to phase out donors' general budget support. There is therefore a particular challenge in Kosovo to accelerate economic reform and the development of the private sector to create growth in the economy and income for government".

In 1999, UNMIK legalised the use and possession of foreign currency in Kosovo, recognising the fact that Kosovo is a largely cash-based economy with the deutsche mark being the preferred currency. As a consequence, Kosovo will change over to the Euro at the beginning of 2002. UNMIK decided that it would follow the model of the EU area with only two months of dual circulation. In this context, it co-operates with the German and Austrian Central Bank and a number of commercial banks. The ECB approved a frontloading also in the case of Kosovo.

The Deutsche Mark/Euro was introduced as a parallel currency in the Republic of Montenegro in late 1999 and is now the sole legal tender in December 2000. It is therefore no longer allowed to finance public sector deficits through money creation. The Government of Montenegro aims to achieve sustained economic growth through continued monetary stability and conversion to the euro. The dual currency period will last for three months, from 1 January, and agreement has been reached on a significant early delivery of euros before that date.

The new FRY authorities have been progressively devaluing the Dinar to an eventual YuD30/DM by end 2000. As of January 2001, the NBY adopted a managed float system with limited current account-convertibility. The National Bank of Yugoslavia is liberalising further the foreign exchange market and reforming monetary policy instruments.

*Private sector and Banking:* The three entities have been focusing on strengthening the legal framework for the private sector and banking system, making it conducive to the development of a performing domestic private sector, attract foreign direct investment and to foster the development of the SME sector which will be key to economic regeneration. Improving

corporate management through investment in training and human resources development is also deemed critical to the future economic growth.

In the area of privatisation, significant progress was made in Serbia with the adoption by Parliament in June 2001 of a new legal framework for the privatisation of large state and socially owned enterprises with transparent procedures over the next four years, emphasising privatisation through public tenders to strategic investors. A first group of 40 enterprises was selected for privatisation in 2001. The Serbian government also identified 28 large loss-making companies for organisational and financial restructuring.

In Montenegro, the extension of the privatisation programme which started in 1991 is the main expression of the Government's commitment to market-oriented reforms. The present phase of the programme (Mass Voucher Privatisation) covers 191 companies and is expected to be completed in autumn 2001. In addition, 110 enterprises are in the process of being privatised through "batch" sales, tenders, auctions, or bankruptcy procedures. Tenders have already been requested for the telecommunications and Electricity Company and a new legal basis has been established in mid-2001 to set up a Regulatory Agency for telecommunication and electricity.

After some delays, the overall strategy on privatisation has been agreed within UNMIK in Kosovo. It is based on a multi-faceted approach which envisages spin-offs, transformation of Socially Owned Enterprises, bankruptcy and liquidation of non-viable enterprises.

The federal authorities made important first steps toward restructuring of the banking sector in the Republic of Serbia that suffers from a lack of financial inter-mediation, bad loans and illiquidity. Based on a survey conducted by the NBY, 28 banks that had been classified as insolvent were re-examined in depth and re-categorised. In mid-July, the four largest banks out of this group (Beobanka, Beogradska Banka, Investbanka and Yugobanka) that account for 70% of the assets of the banking system in the FRY, were transferred to the newly established Bank Rehabilitation Agency (BRA) that will develop rehabilitation plans.

Further changes in the legal and regulatory framework are envisaged to strengthen the banking system. The legal basis to allow the BRA to perform the functions of a liquidator has been adopted and is expected to considerably speed up the bank restructuring process.

The new laws on the Central Bank of Montenegro and on the Banking System were adopted by the Montenegrin Parliament in November 2000 and the authorities started the implementation of these laws, which are in compliance with international standards and should provide the basis to transform the current cash economy to a market oriented system of financial inter-mediation. Progress has also been made in the field of banking supervision and restructuring. The main commercial bank (Montenegro Banka) has been placed under temporary administration and will be liquidated or restructured without injection of public capital. In parallel an action plan for the reform of the payment system was adopted by the Government and is being implemented. A new foreign bank started operations in early 2001 and requests for licences from three other foreign institutions are under review by the authorities."

After a slow start, the development of the financial sector is gaining speed in Kosovo. The Banking and Payments Authority of Kosovo (BPK) has granted final licences to 7 banks which are now operating in Kosovo and 15 non-bank credit institutions (essentially providing donor funded micro-credit schemes). The lending activities of banks are expanding and the number of non-cash transactions are growing albeit both from a low level; however, Kosovo continues to be a largely cash-based economy. Since 28 September, the BPK has been responsible for the licensing and supervision of foreign exchange bureaux and money transmitters; by end of November, one foreign exchange bureau and five Western Union operations had been licensed. The BPK has taken over the responsibility on insurance licensing, supervision and regulation (regulation 2001/25 of 5 October 2001).

*Energy:* The stabilisation of energy and its long-term security are basic pre-requisites for the overall economic reconstruction process and the general welfare of the beneficiary population. Therefore, the rehabilitation of essential energy production and distribution capacities stands at the forefront of the Federal Republic of Yugoslavia's energy policy. To that aim, the pertinent regulatory framework must be substantially amended and aligned with EU standards. Moreover, the authorities will target energy efficiency investments, and introduce appropriate pricing policies (including an improvement of billing and collection rates). Finally, the integration into the regional energy grid as well as into the wider Trans-European networks is of vital importance.

*Transport:* The availability of functioning transport infrastructure in all its forms is the key to sustainable economic growth in South Eastern Europe and its linkage to the European Union. As a first priority, the FRY authorities have decided to reconstruct existing transport infrastructure. In a second phase, long-term strategic connections shall be established and market access for operators in the various transport sectors shall be liberalised. In addition, the respective regulations and standards (including safety and environmental legislation) will be brought in line with EC law. Regarding railway transport, the FRY plans to separate transport operations, infrastructure management and regulatory functions.

*External economic policy and International organisations:* Since the end of 2000, the FRY authorities have been able to normalise external economic relations, including re-establishing links with International Financial Institutions.

The resumption of IMF membership took place in December 2000. In the first half of 2001, the FRY became a member of the EBRD and the World Bank. A decision to include the FRY in the guarantee mandate for external action of the EIB was reached on 6 November and paved the ground for EIB intervention in financing infrastructure projects starting with transport. .

Not being a sovereign state, Kosovo is having difficulties in obtaining support from International Financial Institutions and may not benefit from conventional IMF or World Bank supported programmes until a solution for guaranteeing loans is in place. However, since the end of the conflict, IMF and World Bank staff have been providing technical assistance and policy advice. It is essential that this issue is addressed if Kosovo is to benefit from the extensive support these agencies can provide. *Trade:* The federal Parliament passed in May 2001 new foreign trade, customs and customs tariff laws aimed at liberalising the foreign trade of the country, to meet the pre-requisites necessary to join WTO and, eventually, implement an SAA with the EU. Most licences and quotas for imports have been abolished although some quotas are still in place on the export side for some strategic agricultural products. The number of duty rates (previously 38) has been reduced to 6 (1,5,10,15,20, 30%) and the average tariff rate is lowered from 14.43 to 9.37%.

### **2.3 Social welfare and Civil Society**

*Social welfare:* The FRY pension system, which is under republican responsibility, is financially unsustainable. As pressure will increase with economic restructuring, the authorities' policy is to redefine the pension and social welfare system and establish a special ad hoc mechanism to alleviate the social consequences of reform. In Kosovo, a major social policy reform agenda has been developed by UNMIK, with the support of the World Bank and the UK. It provides the basis for future development for the range of social welfare and social services in the province.

*Health:* The health care sector is in crisis and the FRY Governments' policy agenda is to reduce its currently unsustainable burden on public expenditure while ensuring service delivery to the most disadvantaged. Measures that will be examined include modernising regulatory frameworks for financing the health system, re-launching the pharmaceutical sector, measures to improve policy formulation, public health management, investment to modernise health delivery and training of physicians and paramedical staff.

*Education:* The low level of resources dedicated to the education sector has seriously hampered its effectiveness. The authorities' policy agenda focuses on the modernisation of all levels of education, especially upgrading the importance of vocational training which is considered essential to meet the future needs of the economy and to reduce unemployment.

*Poverty alleviation:* The FRY Governments' policy agenda is to target scarce public resources on the most vulnerable poverty groups in society. This targeting involves the development of better statistics on vulnerable poverty groups, building capacity in the local social welfare network and training staff in modern welfare techniques. In Kosovo, UNMIK intends to reflect the analysis and conclusions of the World Bank Poverty Assessment report. The World Bank is discussing with Serbia and Montenegro the planning of a Poverty Assessment that would provide the basis of an eventual full Poverty Reduction Strategy. This, with the Poverty Assessment developed for Kosovo, will be an important tool for the implementation of the CARDS programme.

*Refugees:* A Task Force has been set up by the *Serbian* government to deal with the issue of integration and support to refugees largely from BiH and Croatia and to displaced persons from Kosovo. As around 60% of refugees have expressed their intent to remain in Serbia, the policy is to design programmes for the integration of refugees without deepening social inequalities with the general population. Another priority is the return of displaced people to Kosovo which will have to be closely co-ordinated with UNMIK, from the security and economic perspective.

### **3 COUNTRY ANALYSIS**

#### **3.1 Political Situation**

The Federation is based on the 1992 Federal Constitution which confers most governmental competences onto the two constituent republics of Serbia and Montenegro. Article 77 of the Constitution spells out the Federation's responsibilities in the fields of human rights (including the rights of minority ethnic groups as well as those of individuals), financial management (including monetary policy, fiscal policy and economic dealings abroad), customs, foreign policy and defence, as well as social welfare and environmental protection.

However, in the final years of the Milosevic regime, this federation system did not function normally.

The two constituent Republics each have their own Constitutions, Presidents and Government structures. While not unusual in a federal system, the distribution of competences between the federal and republican levels in the FRY - and the numerous incoherences and contradictions between the constitutions - is unusual, reflecting the offices held by Milosevic at the time each key document was drafted. In practice, the republics have more powers than the federation itself not only through the constitution but also in their "de facto" exercise of some of the competences that should at least officially be exercised at the federal level.

The current governing coalition in Montenegro is not represented in the Federal Parliament due to constitutional changes in July 2000 followed by their boycott of the September 2000 federal elections.

The restructuring of the federal state and revision of the federal constitution are among the elements to be discussed in the dialogue between the republics. The proposals for a restructured state would leave only a limited set of competences at federal level.

*Kosovo* has been under international civil (UNMIK) and military (KFOR) administration since June 1999, in accordance with UN Security Council Resolution 1244. At present, UNMIK activities comprise four "pillars", dealing with justice and police issues, civil administration, democratisation and institution-building and, lastly, economic reconstruction and

development, the latter being under EU lead. These pillars oversee a joint interim administrative structure (JIAS) as well as the municipal-based administrative councils and boards. In addition, the Interim Administrative Council (IAC) and the Kosovo Transitional Council (KTC) represents the full spectrum of society and political parties. These various bodies are being replaced after the 17 November 2001 Kosovo-wide elections. Kosovo is now entering a new era in which responsibility of government will be shared between UNMIK and the elected representatives through the institutions of provisional self-government<sup>4</sup>.

On the Federal and Serbian side, the main short to medium-term concerns are for the safety of Kosovo Serbs in Kosovo and for conditions to be established to permit the return of those IDPs currently in Serbia proper. Since mid 2001, UNMiK has a liaison office in Belgrade which works for a greater understanding of the role and work of UNMIK in Kosovo and encourages a dialogue between the authorities of the Province and those of Serbia and the Federation. This dialogue has been reinforced by the signature on 5 November 2001 of an UNMIK-FRY Common Document, which reaffirms the will of both parties to co-operate to ensure the full implementation of UNSC Resolution 1244.

The poor human rights' record of the previous Milosevic administration will long be felt. Under this regime, numerous abuses were recorded by the politicised police, including forced displacement, torture and killings. Fairness of trials was not ensured and the politically dependent judiciary suffered a high degree of corruption. Prison conditions did not meet international standards. Addressing these problems will take time.

Inter-ethnic relations must also be improved. Minorities, including the Roma, face discrimination and their basic rights are still not fully respected. Inter-ethnic violence is still very acute in Kosovo. The rights of return for refugees and displaced persons has not been secured throughout the territory of FRY and returnees frequently suffer from discrimination in respect of their civil, social and political rights. Gender discrimination is still an issue that requires attention. Trafficking of human beings and illicit goods are serious problems.

Yet the change in government in Serbia had immediate, positive consequences on the freedom of association, of expression, of movement, and on academic freedom. Freedom of press improved also, although media independence and professionalism still needs to be improved as political influence is exercised over wide sections of the media.

Democratic reforms, including in particular the establishment of the rule of law, respect for minority rights as well as inter-ethnic reconciliation, and respect for international obligations, notably full cooperation with the International Criminal Tribunal for former Yugoslavia (ICTY), are among the main challenges for the State, compliance with which will be closely monitored by the European Union as these are key elements in the "conditionality" governing the EU's Stabilisation and Association Process

### **3.2 Economic Situation**

The economic effect of a decade of wars, sanctions, unsustainable economic and financial policies, de-industrialisation and international isolation have been very damaging for the FRY. Its economy (without Kosovo) registered between 1990-1999 a negative average annual growth rate of 7%, leading to GDP in 1999 being about half of that registered in 1990.

The FRY's entities have started the necessary reforms to reverse this damage. The 2001 Economic Reconstruction and Transition Programme sets out the broad reform package to 2004, as well as indicating key government and donor activities to be undertaken.

However, the transition to a market economy is taking place under extremely difficult economic and social conditions. Assistance from the EC and other donors is being provided,

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<sup>4</sup> UNMIK Regulation 2001/9 of 15 May 2001.

to alleviate the plight of the poorest members of society. Such significant and swift emergency assistance has been key in ensuring stability and enabling the country to undertake its reforms, as shown by the support that helped the government through the very difficult winter of 2000-2001.

The lack of reliable statistical sources make it difficult to quantify current economic developments. GDP per capita in 1995 was unofficially estimated at €539 and tentative estimates indicate this has risen to some € 800 in 2000. Workers' remittances from abroad remain a major source of household income.

FRY's macro-economic situation is a source of deep concern for the country's future stability. The public finance system of FRY was undermined in the past decades by ill disciplined fiscal activities and inflationary monetary policies. Debt arrears total some US\$12.2 billion, far exceeding the country's servicing capacity for the foreseeable future. In the medium term, FRY will continue to rely heavily on external financial assistance, including debt relief.

In November 2001, the Paris Club of creditors decided to write off 66% (US\$ 3 billion) of FR Yugoslavia's US\$ 4.5 billion debt. 51% of the debt will be written-off upon signing a new Stand-By Agreement with the IMF in March/April 2002 and the further 15% written-off in 3 years when that agreement expires. As for the remaining portion of the debt (approx. US\$ 1.5 billion), an agreement has been reached on rescheduling this debt for a period of 22 years, with a 6-year grace period. The payment of the major part of the interest (60%) will also be postponed (accruing to the principal), while the remaining 40% should be repaid in the next three years (US\$ 30 million in 2002, US\$ 50 million in 2003 and US\$ 60 million in 2004). Next in line are negotiations with the London Club on US\$ 2.8 billion debt and it is expected that the write-off should be of a similar level.

FRY authorities have moved rapidly to forge closer relations with regional trading partners and has applied to join the WTO. Not only will trade liberalisation be key for the FRY's economic recovery and development, the policy and institutional reforms required to join the WTO should mirror the economic preconditions under the SAP process for a Stabilisation and Association Agreement – the key document permitting closer association of the FRY to the EU.

*Republic of Serbia:* The Government planned to tackle the 2001 budget deficit with privatisation revenues (YuD 10 billion) and donations/loans (YuD 12 billion). However, delays on establishing the new privatisation framework with transparent procedures and delays on particular privatisation deals (eg. three cement companies in 2001) continue to constrain the Serbian Government's ability to deliver sufficient basic public services such as energy, infrastructure and social protection. With current price liberalisation measures, there has been additional inflation in 2001 on top of the 113% experienced in 2000. However, there are also very positive achievements so far as demonstrated by the considerable reduction of monthly inflation despite price liberalisation, the maintenance of exchange rate at 30 YUD/DM and the considerable improvement of the exchange reserve position since the new government took over. A budget cash surplus has been achieved in the first half of 2001.

The short term results of the economic restructuring process, with frozen salaries and redundancies, may lead to an increase in social pressures. As a result, while the Government remains committed to structural reforms, it may be forced to slow down the pace of such reforms to alleviate unrest.

FRY/Serbia – Main Economic Trends					
		1997	1998	1999	2000
Real GDP growth	%	7.4	2.5	-15.7	6.7
Inflation rate	Average in %	18.5	29.8	42.4	73
	Dec-on-Dec	9.3	44.0	50.0	113.0

Unemployment	% of labour force	25	25	27	27
Government Budget Balance	% of GDP	na	na	na	0.2-0.4
Current Account Balance	% of GDP	na	-5.5	-7.5	-8.3
Gross Foreign Debt	USD billion	na	na	na	12.2
Debt-to-Export Ratio	%	na	na	na	450
Foreign Investment	USD million	740	113	112	25
	% of GDP	4.7	0.9	0.9	0.3

Sources : IMF, FRY government

*Kosovo:* Economic activity has resumed with considerable speed after the conflict and living conditions continue to improve. It is also being extensively funded by remittances from the ethnic Albania diaspora. There has been a noticeable increase in the number of small and medium size enterprises engaged in economic activities, predominantly small trade. Agricultural production in 2001 is estimated to have regained its pre-war level. Construction and some trade-related services are booming. Industrial production appears to be still very low, but employment and fixed assets have increased substantially compared to 1999 and business confidence appears high. The post-war recovery is likely to continue as the construction boom will persist in the short-term, largely driven by the major international donor-funded reconstruction program. It is essential for Kosovo's future economic prosperity that significant foreign and domestic investment substitutes for donor funds and for dependence on remittance income. For foreign investors to have confidence in Kosovo, there needs to be a clear and constructive relationship with Belgrade in particular.

The temporary customs regime remains the main source of revenue with 10% tariff and 15% sales tax in place (replaced by VAT in June 2001 at the same fiscal levels). This has been complemented by car registration tax and a business tax on hotels, restaurants and bars. UNMIK's medium-term fiscal strategy acknowledges the necessity to make progress towards a self-financed budget, to increase budget sustainability and to reduce donors' general budget support. In the course of 2001, revenues (including donor funds) have been better than expected reflecting economic growth and increased compliance. It is now time for the budget to mature and take on other types of expenditures such as maintenance and other capital expenditure, especially against the background that donor funds for these types of expenditures are declining. However, the budgetary situation in Kosovo remains vulnerable to external factors. Less successful has been the cost recovery in investment-thirsty public utilities such as electricity, water and waste companies. For electricity, only 30% of the people and enterprises were successfully billed in 2000 and only 30% of them actually paid their bills.

*Republic of Montenegro:* Montenegro suffered less from international economic sanctions but economic activity has constrained in 2000-2001 by the disruption of trade with Serbia. In addition, budget execution is still a cause for concern with over-spending and inadequate revenue collection leading to large fiscal imbalances in 2000. Public spending has risen due to a boost in wages for public sector employees and in social benefits related to wages. These amounted in 2000 to two thirds of total expenditure of the Republic's budget. The consolidated general government deficit was mainly financed through international financial assistance and also through accumulation of new arrears. The 2001 budget foresees a reduction of the deficit but the deficit will probably continue and need to be covered with support from the donor community.

The government is committed to a gradual lifting of price controls for basic foodstuffs, communal services and other goods, which previously had been subject to administered pricing.

		1997	1998	1999	2000
Real GDP growth	%	6.5	-1.5	-14.0	4.0-6.0
Inflation rate	Average %	23.4	32.4	67.4	97.0
	Dec-on-Dec	...	41.8	146.0	22.5
Unemployment	% labour force	23.5	25.7	27.3	29.4
Government Budget Balance	% of GDP	...	...	...	- 16.6
Current Account Balance	% of GDP	...	...	...	12.5
Gross Foreign Debt	USD billion	...	...	...	0.567
Debt-to-Export Ratio	%				230
Foreign Investment	USD million	...	...	...	...

Sources: IMF, Monet, Montenegrin Government

*Public utilities and Infrastructures:* Energy generation and distribution has been seriously affected by a mixture of conflict damage and under-investment. The energy exchange from one entity to another and with neighbouring countries to compensate for any shortfalls is not efficiently managed. Oil and gas play a significant role in energy production in Serbia. Due to price and environmental considerations, natural gas has a potentially important future to play in Serbia whilst in Montenegro and Kosovo coal fired power is still economically the most viable option at present. District heating systems which cover parts of major towns in the FRY is an important alternative to electric heating. Originally sophisticated water and sanitation systems are now often derelict. Moreover, the utility sector suffers from innumerable leaks and losses, inadequate pricing policies and wastage.

Large investments will be required from the donor community, IFIs and the commercial sector to get this part of the sector fully operational.

In addition to extensive rehabilitation needs to existing water systems, there are complex institutional arrangements inherited from the SFRY which also need to be radically revised. Currently, administrative borders and water utility coverage areas do not correspond and whilst most utilities have a municipal focus, there are several regional water supply systems that serve more than one municipality. These municipal companies are usually overstuffed, inefficient and lacking in modern management techniques.

Ground water quality fell to unsatisfactory quality levels due to the increasing amount of poorly run municipal and industrial waste sites and ad hoc fly-tipping creating particular problems in the coastal and larger cities. The recent conflict has also left its environmental scars with toxic emissions from heavy industries struck by missiles. Industrial wastes dumped into the Sava which flows into the Danube as well as sewage outlets in tourist areas (e.g. Kotor) and air pollution (e.g. Belgrade) are important environmental concerns. Lack of maintenance is the primary reason for the degradation of the road networks in FRY with only 25% of main and regional roads in good condition in Serbia and even lower figures for Montenegro and Kosovo. This leads to slow and expensive road transport and safety risks. Recovery costs in FRY which could allow for maintenance are hopelessly inadequate and completely absent in Kosovo.

The same problems have affected the largely entity-run FRY railway networks with similar consequences in terms of poor management, inadequate maintenance and asset renewal, with wagons and coaches generally being around 30 years old. Maritime transport only concerns the Port of Bar in Montenegro which is a sufficiently well equipped facility currently only running at 20% of potential capacity despite handling 95% of all FRY's maritime trade, totalling 1.3 million tonnes in 2000. Aside from pure maritime transport, one has to consider river transport which was affected by the NATO bombing campaign. There is much potential here as river transport is considered as a highly economical and environmentally friendly mode of transport for heavy goods.

*The private sector:* The last decade of conflict, sanctions and economic isolation has played havoc with the development of enterprises and commercial banks through the loss of markets and business contacts, missing out on technological advances and modern management techniques and delaying the introduction of modern, market oriented ownership structures which had begun to emerge in the 1980s. Compounding these problems, the 1990s also saw repressive laws and regulations encouraging the growth of the grey economy and deterring inflows of investment and working capital to enterprises.

Industrial production has fallen drastically over the last decade by 60% with most enterprises operating at under 30% of their capacity. The enterprise sector has been de-capitalised and seen much of its assets rendered obsolete. Moreover, many enterprises have seen their compliance on environmental protection fall further behind EU norms and will need a long time to catch up.

The Kosovo conflict complicates matters further due to damage and vandalising of a number of key enterprises in the metallurgy and chemical industries.

State and Socially owned (SOEs) and mixed ownership enterprises dominate the enterprise sector in FRY in terms of numbers of workers employed by a ratio of 6:1. In SOE, workers collectively hold ownership rights of the enterprise in terms of management choices and the rights to dispose of assets and residual income. Privatisation has evolved at different paces in the three entities due to opportunities provided by the recent past. Montenegro has had a mass privatisation programme since 1991 and the process has accelerated since 1997, although still only 7% of assets have been privatised. In Kosovo, the process applied to SOEs is that of commercialisation through ten year take-overs of viable companies by foreign enterprises, as the only practical way forward due to the complex legal situation. However, UNMIK plans to set up the Kosovo Trust Agency (KTA) to administer SOE's in Kosovo. In Serbia, the process has barely started. Foreign direct investment remains negligible throughout the FRY.

In private sector development, the promotion of SMEs is currently weighed down by burdensome bureaucracy and regulations governing their operations. The commercial banking sector needs to be improved in order to provide competitive financial services.

Agriculture which has always been a central part of the FRY economy (22% of GNP in 1999) is also suffering from a lack of incentives for production and export, as well as from a shortage of capital resources. The public institutions and agencies which support the sector are ill-equipped and ill-suited for helping the sector move towards a market economy.

### **3.3 Social situation**

There are major problems of social policy and social cohesion throughout the FRY, relating to employment and education, labour markets, health, social protection and the role of civil society. There is a major challenge to maintain social cohesion as economic competitiveness increases.

Welfare benefits are based on an overly complex system which needs to be rationalised and have its coverage broadened, especially in the light of future price liberalisation and refugee integration. The delivery of welfare benefits is further affected by an under-equipped delivery network and often inadequate physical infrastructure.

Unemployment in FRY is high - 730,000 registered as unemployed in Serbia, 85,000 in Montenegro and around 60% unemployed in Kosovo. However, unemployment benefit coverage is low - 6.5% in Serbia and 4% in Montenegro, and only 50,000 of the most vulnerable in Kosovo covered. Labour market laws need major modernisation.

Education has suffered from budgetary cutbacks with an exaggerated but under-paid work force. An effort to rationalise and upgrade education facilities needs to be made. In Kosovo, due to the many years of a parallel system for Albanians and the running-down of Pristina

University, efforts have to start from a low base line. Educational needs of minorities and access to education - in particular in the enclaves - requires further attention.

Health has also suffered from budgetary cuts and years of mismanagement. Consequently, the delivery of an effective and efficient health care to the population has substantially deteriorated with many health facilities in poor condition and pharmaceuticals expensive and hard to obtain. The FRY authorities have requested support to health sector reform. The World Bank has indicated that there is need for donor support in this area before its own programmes begin in 2003.

In Kosovo, the most pressing health needs of the population have been addressed by ECHO. Subsequently, a CARDS funded health sector reform programme is now under way which also tackles the outdated qualification of health professionals. However, there are still difficulties in health delivery to minorities.

The large amount of refugees and displaced people living in Serbia and Montenegro is a potential source of social tension, especially if unsettled political conditions in the wider region continue. In Kosovo, the Joint Committee on the Return of Kosovo Serb (JCR) has established a "Framework for return 2001" which identifies the measures required to create conditions conducive to IDP's and refugee return. However, despite UNMIK, KFOR and UNHCR's efforts, security conditions and sustainability concerns still remain.

As the humanitarian organisations gradually phase out from the FRY, the social welfare systems will have to cope with a situation further aggravated at least in the economic transformation period.

### **3.4 Capacity for European Integration**

Participation in the European integration process will place political and economic demands on the FRY which the country has so far only a limited capacity to address.

In the political area, FRY's capacity for European Integration will be assessed by reference to its ability to secure democratic principles, the rule of law, respect for human rights and the protection of minorities. In addition, a fundamental issue presently lies in the path of Yugoslavia and its constituent entities' aspirations for EU integration: a clear definition of the State. The current uncertainty of Kosovo's final status and Montenegro's position within the Federation affects its capacity to fulfill the requirements for rapprochement to the EU and progress within the SAP.

The FRY's new found democracy, although promising, remains fragile and yet to be consolidated. Institutional weaknesses in the public administration will need to be overcome quickly as European integration demands an important capacity to meet the legislative, regulatory and enforcement challenges which the process entails. Kosovo faces a particular challenge with the arrival of the provisional self- Government that will be elected in late 2001. It is clearly essential that all entities and all relevant authorities within the entities are full participants in the Consultative Task Force and that reform measures taken in Kosovo are fully consistent with the SAP.

Justice and Home Affairs is also a key area of concern as the Balkans has been identified as a hub for illegal trafficking. The normalization after years of conflict in the region has unfortunately led to the increase of illegal traffic in particular, in human beings as earlier experienced also in the Candidate countries. FRY has become a transit country for illegal migration directed towards the EU. Alignment with EU visa and entry policies, and combating organised crime effectively is necessary.

While most major parties and governments share the goal of European integration there is little real appreciation of what the process actually involves. With few exceptions, there is scant knowledge of the Community acquis and the administration does not have the ability to

formulate policy and draft legislation consistent with it. In addition, as regards implementation of legislation and standards, there is a severe lack of monitoring and enforcement capacity.

The economic issues relating to increased European integration have been dealt with in sections above. However, it is worth recalling the fundamental importance in the European integration process of a functioning single market for the FRY on the basis of the EU model, of a harmonised external trade regime for the FRY and of the full respect of human rights and democratic principles which is presently not the case.

### **3.5 Sustainability of current Policies**

Throughout the FRY there is a need for major programmes of public sector transformation, physical and economic rehabilitation and social policy reform. This will require effective donor co-ordination.

The FRY governments and local authorities have been focusing efforts on the foreign policy agenda, conscious of the need to integrate the FRY back into the mainstream of international politics and economics and turn the past of last decade's isolationism. Concretely this has led to the re-integration of the FRY with the IFIs and various supra-national bodies.

This is a promising start but should not detract from the need to resolve, in parallel, domestic policy issues such as public administration reform, private sector development, justice and home affairs and a strengthened civil society. These are areas where positive steps have already been made but which will require more substantive progress in future, despite the unpopularity of certain reforms which may become apparent in particular during economic restructuring.

The social situation can be described as reasonably stable, compared to recent years, but with great potential for volatility. The incidence of poverty is very varied from Serbia to Montenegro to Kosovo but is generally concentrated in rural zones and areas of high refugee population or ethnic minorities as well as among pensioners and the unemployed. This precarious social situation may lead to political dissatisfaction.

It is essential that while these issues are addressed, the SAP is applied across all areas of the FRY. It is a significant unifying factor for economic and social reform, promoting sustainability.

### **3.6 Medium Term challenges**

Seven medium term challenges emerge from the above analysis that need to be tackled if FRY's political, economic and social development is to be assured and sustainable.

*The clarification of the Federal state:* The challenge for the federal, Republic and Kosovo authorities will be the clarification of political and institutional arrangements within the Federation. A new platform, to be consolidated into a reformed constitution, will be required to firmly establish a workable and efficient system of governance inside the federation.

*Establishing the single economic space:* The priority without prejudging any final political solution on the FRY must be the creation of a single economic space. This will require harmonisation between the three entities of policies and procedures and movement towards models of best practice as established in the EC Single Market, particularly in the fields of freedoms of movement and establishment, central and commercial banking, customs and taxation, privatisation, trade, price liberalisation and currency. A continued lack of convergence in these fields can only harm the development of the country as a whole and place unnecessary obstacles in the path of the SAP process.

*Resolving the macro-economic situation:* The legacy of past fiscal imbalances and accumulation of domestic and external debts has left the FRY in a highly vulnerable condition. This is likely to be compounded by the servicing of the external debt while

pursuing economic restructuring, placing added pressure on FRY's fragile external accounts. This can only be resolved through sound and sustained macroeconomic management, key structural reforms and well targeted foreign assistance. For Kosovo in particular, the quasi-fiscal deficits of the budget relating to the lack of fee recuperation from public utilities represent the most immediate worry, along with the widening of the tax collection base.

*Alleviating poverty:* With 12% of the FRY population living in absolute poverty, increasing the standard of living and promoting employment is a key to upholding the new democratic regimes in the FRY and ensuring internal stability. At the same time, as the humanitarian organisations are reducing their involvement in the FRY, there is a risk that the most vulnerable layers of the population who may not benefit so quickly from the early phases of the economic recovery, will be further impoverished.

*Promoting good governance, democracy and civil society:* Education, public administration and judicial reforms are fundamental for good governance and ensuring the basic rights of the individual. One of the foremost and most problematic challenges in this area is the amelioration of inter-ethnic relations which must be sensitively managed with respect to the cultural, administrative, political and economic rights of all ethnic groups. Relations with minorities must be worked on, through confidence building, integration and resuming political dialogue.

The media must be upgraded both in terms of quality and politically independence. Conduct during the recent elections in Montenegro demonstrated the continuing degree of government control of the media. In fostering the independence of the media, attention must be given to public service broadcasters so as to ensure a pluralist and reliable source of quality information for all.

Civil society has played a key role both in terms of struggle-oriented movements and as a service-provider responding to the failure of delivery by the public sector. However civil society suffers in many cases from a lack of organisational capacity and strategic vision. Civil associations and non-governmental organisations need to be provided with the right environment and the means to become efficient and effective organisations so that they can continue to play the watchdog function on public institutions and engage increasingly in debates of national importance.

*Strengthening the public administration:* The main priority is for the State to recover the capacity to deliver on its main functions in a transparent and accountable fashion. Reform of the public administration (as a pre-condition for effective and sound delivery of public services) and of the police and judiciary (so to ensure the respect and compliance with basic rights and laws) are therefore obvious areas of priority.

*Approximating laws and policies to those of the EU:* The lack of a modern administrative culture and the legacy of the previous government system could hamper the effective implementation of the commitments undertaken under the SAp and, in the future, under an SAA. The focus on the process of legal harmonisation needs to be accompanied by the necessary structural reforms in order to ensure the effective implementation and enforcement of the enacted legislation. The SAp itself, and the progress made by the FRY towards negotiating an SAA, will be monitored regularly. The country will have to demonstrate the capability to engage in reforming a highly centralised and politicised public administration.

*Fostering participation of International Financing Institutions:* Aside from the difficulties in relation to the outstanding arrears, IFI's are presently preparing substantive investment packages for future involvement in the FRY. The particular status of Kosovo will require a very creative approach to solve the outstanding issues in the areas of debt sharing, resolution of ownership rights and privatisation/liberalisation policy frameworks, to allow for a larger involvement of the IFI's in financing investment opportunities in the province. Thus, the Federal authorities on one hand and UNMIK and the Provisional for Institutions for Self-

government have to engage in a constructive and mutually beneficial dialogue to ensure that loan-financing can start as soon as possible to bridge the phasing out of EC assistance in the investment sector as of 2003.

## 4 PAST AND ONGOING COOPERATION

### 4.1 EC Programmes: past and present

In the FRY, as in the whole of South Europe, the European Union is making a substantial contribution, in political, military (in the case of Kosovo) and above all financial terms to building lasting peace and democracy.

With a substantive amount of European Community funds at its disposal and making use of a wide range of financial instruments, the European Commission has successfully supplied humanitarian and emergency assistance, has supported refugees and IDP's, fostered democratisation and independent media, encouraged financial stability, supported the economic recovery and physical reconstruction of the FRY and has helped lay the foundations for FRY's advancement in the Stabilisation and Association Process with the view of future European integration.

An overview of EC funded assistance to the Federal Republic of Yugoslavia can be found in Annex 3.

The European Agency for Reconstruction is responsible for the management of the main CARDS assistance programmes implemented in the FRY. In Serbia, the bulk of the EC non humanitarian intervention to date has focused on the energy, agriculture -including food and fertiliser supplies, health, municipalities (towns and school for democracy) and media sector. In addition, since 1992, the humanitarian instrument of the Commission has been active in Serbia providing assistance to refugees and IDP's (since the Kosovo crisis) as well as to the local population through social and health programmes. In Montenegro, assistance has been concentrated on administrative reforms, including exceptional budgetary support, agriculture, transport infrastructure and enterprise development. ECHO has mainly focussed on the provision of basic humanitarian assistance, self-reliance projects and the health sector. A wide range of assistance has been provided to Kosovo since the aftermath of the conflict. ECHO provided emergency humanitarian assistance followed by the rehabilitation type activities in shelter, agriculture, health, education facilities, rural infrastructure and self-reliance projects. The European Agency for Reconstruction has concentrated its efforts on the energy, housing reconstruction, infrastructure rehabilitation, water and environment, social, including exceptional budgetary support and civil administration support, enterprise development, health and agriculture have received significant attention. Implementation of CARDS programmes managed by the Agency are well advanced, with an average 80% contracting rate and 60% disbursement rate.

<b>Cumulative CARDS Assistance by Sector (1998-2001) - Indicative allocations</b>	<b>Serbia</b>	<b>Kosovo</b>	<b>Montenegro</b>
<i>Justice &amp; Home Affairs</i>		9,0	
<i>Customs</i>	5,0	13,9	1,4
<i>Public Admin</i>	5,0	47,6	24,2
<i>Energy</i>	211,0	273,1	2,5
<i>Transport &amp; Infrastructure</i>	30,0	39,3	20,7
<i>Water &amp; Environment</i>		44,7	
<i>Economic Development</i>	20,0	33,5	4,2
<i>Agriculture</i>	46,0	41,3	3,3
<i>Housing</i>		111,8	
<i>Health + Social</i>	51,5	54,0	
<i>Education</i>	7,7	4,3	5,1

<i>Civil Society &amp; Media</i>	10,1	19,4	0,8
<i>OTHER (running costs, Technical assistance facilities, etc)</i>	16,6	37,6	5,3
<b>TOTAL</b>	<b>402,6</b>	<b>729,5</b>	<b>67,4</b>

Further details on the scope of past EC assistance provided under the CARDS programme to the FRY can be found in the annual report of the European Agency for Reconstruction.<sup>5</sup>

#### **4.2 Constraints/Problems/Lessons learned/Recommendations**

The creation of the European Agency for Reconstruction was designed to improve the efficiency and effectiveness of the massive EC assistance provided for the reconstruction and recovery of Kosovo and, from December 2000, for Community assistance throughout the FRY. The Agency, has been able to act as a high quality and fast delivery mechanism whilst ensuring transparency and control in its operations, as evidenced in the positive report from the European Court of Auditors<sup>6</sup>.

EC assistance operations in Kosovo and now FRY/Serbia have benefited from the lessons learned in the case of similar operations in the region, particularly in Bosnia and Herzegovina. Lessons learned which have helped steer programmes in the FRY include:

- The importance of concentrating funds on a limited number of key sectors in order to ensure maximum impact with the resources available. Early operations in Kosovo concentrated on only four sectors which were the basis of any future developmental efforts (ie. energy, water, housing and transport).
- The importance of ensuring maximum co-ordination with other EC programmes and other donors to promote leverage, to ensure a harmonised approach to the reform process and to avoid any overlap or gaps in support. CARDS/Obnova assistance in Montenegro was used successfully in conjunction with macro-financial support from DG ECFIN and DG DEV on such issues as price liberalisation.
- Great importance has been given to stringent prioritisation, of analysing the risks involved in a given intervention and of defining precisely necessary accompanying measures required for an intervention to be successful. Assistance to Serbia during Winter 2000-2001 had to assess correctly what essential elements were required to help people survive the harsh winter and defuse social unrest (i.e. energy, food and pharmaceuticals).
- In situations resulting from violent conflict or instability (i.e. Kosovo and Presevo area), or where a humanitarian crisis has taken place, it is important to co-ordinate efforts on humanitarian assistance, conflict management and resolution measures as well as reconstruction and long-term structural assistance so as to effectively link relief, rehabilitation and development interventions. (e.g. a good example has been set in Kosovo, in terms of co-ordinated EC action between ECHO and the EC TAFKO/EAR).
- The importance of finding the right balance between direct physical investments and accompanying technical assistance for institution building measures which will allow the beneficiary sector to operate in a sustainable manner. A good case is the energy sector in Kosovo where institutional arrangements are being worked on intensely so as to protect the massive physical investments to date.
- The importance of working closely with the IFIs so that physical investments become increasingly tackled through loan measures and EC grants can concentrate on institutional reform or through co-financing when critical mass is to be reached.

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<sup>5</sup> COM(2001)446 final of 30 July 2001

<sup>6</sup> Report concerning the financial accounts of the European Agency for Reconstruction and the implementation of aid for Kosovo for the year 2000, 12 November 2001 (ECA/01/32).

- The importance of ensuring true ownership of the assistance offered so that all actions are supported and understood by local authorities. This requires building a strong and efficient interface with the FRY and Republican Governments and with UNMIK.
- The importance of being able to benchmark the progress of a given project, be it at the programming stage, during implementation or ex post evaluations.
- The need to mitigate possible negative effects which can be done to the single economic space through different speed or direction in reform processes in the different entities. The need to ensure that the reform process follows an integrated and co-ordinated approach in all parts of the FRY.

### 4.3 EU member States' programmes

The European Union has pledged some half of all of the assistance identified in the Economic Recovery and Transition Programme for the Federal Republic of Yugoslavia in 2001.

This effort complements the ongoing EC assistance via the emergency package of €200 million launched in 2000 for the Republic of Serbia, the €45 million of EC assistance provided to the Republic of Montenegro and the bilateral assistance programmes of the EU Member States to date.

These figures do not reflect the separate effort undertaken by the EU for the reconstruction and development of Kosovo. By December 2000, more than €1.5 billion had been committed to the province of which two-thirds came from the European Community and the EU Member States. Including the costs of the peace keeping operation in Kosovo, the EU investment in peace and stability for this province amounts to over €8 billion.

Federal Republic of Yugoslavia Donor's Conference Brussels, June 29, 2001		Pledge (In Euro millions *)
EU MS Countries / European Commission		594,02
Austria		33,10
Denmark		8,00
Finland		3,36
France		21,27
Germany		78,23
Greece		53,37
Italy		115,20
Luxembourg		6,50
Netherlands		6,81
Spain		8,75
Sweden		12,83
United Kingdom		16,60
European Commission		230,00
European Investment Bank **		150,00
Total EC+ EU MS + EIB:		744,02
Total 2001 Pledges from all donors		1.568,10
% of total share of EU contribution to the FRY		47,45%

\* 1 Euro = 0.8558 USD (EC Budget Execution Rate for June 2001)

\*\* Subject to approval of lending mandate to FRY by European Council of Ministers

### 4.4 Other Donors' Programmes

The international community and international financial organisations are also contributing very generously to the financial and investment needs of the FRY. In total, they will be taking

on board the remaining 50% of the burden sharing identified by the Economic Recovery and Transition programme for the Federal Republic of Yugoslavia in 2001.

Federal Republic of Yugoslavia Donor's Conference Brussels, June 29, 2001	Pledge (In Euro millions *)
Non EU - Countries	393,65
Canada	13,21
Estonia	0,06
Hungary	3,55
Japan	58,42
Korea	1,17
Norway	21,99
Russia	56,09
Slovenia	0,72
Switzerland	26,23
United States	212,20
International Financial Institutions / Other	430,43
European Bank for Reconstruction and Development	241,00
World Bank	175,27
United Nations Development Program	1,99
UNICEF	6,43
Soros Foundation	5,75
Total:	824,08

## 5 THE EC RESPONSE STRATEGY

### 5.1 General principles and objectives for EC co-operation and assistance

The general principles for EC activity in the FRY and its constituent entities must take account of the complicated current political and economic situation, the constraints and different reform agendas and the need to help the country to move towards the EU.

This section sets out the underlying principles which will guide CARDS assistance formulation and delivery:

The *harmonisation towards the EU acquis* and *rapprochement to EU norms* in all reforms and institution building exercises is an across-the board basic parameter which will be reflected both in all Community support, whether it be the sectoral programmes or support specifically to public administration reform and legislative development associated with FRY's participation in the SAp.

The EC Response Strategy serves not only the direct policy goals of the SAp as required by the CARDS regulation but also two critical objectives underpinning all EC support, namely *conflict prevention* and *poverty reduction*. The SAp is a regional conflict prevention strategy and the EC Response Strategy will address fundamental weaknesses and tensions which may contribute to or trigger conflict within the country and the region. In addition, the SAp is designed to contribute to the stabilisation of the countries of the region and their economies. Sustainable economic development is central to the SAp. All of the measures supported will contribute directly or indirectly to this goal. It is only through sustainable development that poverty reduction can be effectively addressed. This is an approach which is shared with the World Bank.

*The regional aspects:* Regional considerations are very important. These have to be seen on three levels: the FRY as a region itself; the FRY and its relations with its immediate neighbours; and, the FRY with the wider region. EC assistance will not only encourage synergy within the Federation but must be coherent with, and linked to, developments and reforms taking place in the wider region. To this end, synergy will be sought between the assistance programmes financed from the national CARDS budget and the funds available

under the CARDS regional programme. The latter is established to help countries achieve the regional cooperation objectives of the SAP. These are set out in detail under the CARDS Regional Strategy Paper.

*Common priorities:* All entities must adopt the same EU-compatible reforms, whether in parallel or together, not only for objective reasons but also to ensure FRY may draw closer to the EU. Special attention will be given to sectors which represent common priorities to all parts of the Federation. This will enable economic reconstruction and reform without destabilising or prejudging political and institutional relationships within the Federation.

*Complementarity with the IFIs:* There are a certain number of areas where loans are available from the IFIs (World Bank, EBRD, EIB) and which require major and continued investments over a certain number of years (eg energy and transport). In those cases, and unless exceptional circumstances prevail, EC assistance will seek to limit its intervention to the completion of the reconstruction activities already initiated as well as to act as a catalyst for potential IFI loans by helping to prepare feasibility studies and technical designs necessary prior to investments being made, leaving such areas increasingly to the IFI's whose comparative advantage in such areas is clear. In its current status, Kosovo's relationship with the IFIs remains complex and uncertain at present and may not benefit from conventional support by IFI's. The general principle of CARDS support will have to be adapted to this specific situation until a solution is found. However, as the Kosovo programme allocations under CARDS will progressively diminish over the period of the Multi-Annual Indicative Programme, it is important that the authorities reach agreements with the multilateral agencies that enable Kosovo to be included in structural adjustments

## **5.2 Priorities for Co-operation**

Based on the above analysis, the EC response strategy will be geared to— firstly, supporting the FRY's participation and progression in the SAP which, through political and economic stabilisation and increasing association to the EU, are the key's to FRY's long-term prosperity and secondly, continued support for the socio-economic rehabilitation that is key to enabling FRY to pass through its current restructuring and reform stage.

The objective for the European Community will be to support issues which lie at the heart of the Stabilisation and Association process and are of fundamental importance to the region, where the Community can bring added value due to its own experience and its work with candidate countries. Attention will also be given to the consolidation of the sectors in which there has been a substantive EC investment to allow its proper hand-over to the Federal, Republican or Local administrations. Particular focus will be given to institutional strengthening and capacity-building across all sectors, to ensuring sustainability and avoiding aid dependency .

In the economic sphere, priority will be given to the establishment of a single economic space, the link of the FRY within the wider region, to trade development and to facilitate investments in infrastructures and programmes which have an essential impact on general economic growth. This will be done with an environmentally-sustainable approach.

In the social sphere, there are many pressing needs which require substantive funding. However, to avoid dispersion of its limited budget and to maximise the imperative of ensuring impact, EC assistance will concentrate on the mitigation of adverse social consequences of the economic transformation process by (i) support to education, especially vocational training and the university sector, which will promote a better qualified workforce and reduction of unemployment, (ii) assistance to public administration reform in the social sectors and, (iii) continued macro-financial assistance which will contribute to economic stabilisation and reform as well as promoting economic growth and thereby also help to alleviate financial constraints and poverty and offset social consequences of restructuring and reform.

In order to deliver meaningful results that address the major objectives outlined above, EC assistance will be concentrated under three main areas of intervention:

- (1) Support for good governance and institution building
  - (a) *public administration reform* - laws and policies in priority SAp areas, capacity building, support for policy and public investment planning, budgetary transparency, an EU based procurement law, assisting with the decentralisation of authority to municipalities and upgrade the statistical gathering and processing capabilities.
  - (b) *justice and home affairs* - strengthening the rule of law, adoption of laws and policies in line with SAp requirements, upgrading the efficiency of the court system, fighting organised crime, developing a suitable asylum and migration policy and fostering cooperation on terrorism.
  - (c) *customs and taxation* - modernising the services and bringing them into line with EU standards, developing enhanced cooperation for the free circulation of goods and people, improving trade facilitation and taxation compliance, widening the taxation base and combating tax evasion.
- (2) Economic recovery, regeneration and reform, focusing on:
  - (a) *energy* - devising a more efficient energy consumption and exchange system, allowing the domestic generation systems to be improved and help restructure the public enterprises in this utility, ensuring proper billing and tariffication.
  - (b) *transport* - improving the efficiency of transport, facilitating trade flows with neighbouring countries, allowing Republican and local authorities to better deal with maintenance and funding issues and to act as a catalyst for attracting IFI loans and other investments in the sector.
  - (c) *environment* - helping preserve natural assets and avoiding irreversible losses, protecting the population from health risks, helping with the upgrading of solid waste and waste water disposal, approximating environmental norms with those of the EU and of international environmental agreements.
  - (d) *economic development* - reinforcing the relevant laws and policies, capacity building the relevant institutions, supporting integration into the international trading system, allowing internal market reforms, promoting SMEs and its finance and restructuring of key, viable SOEs, alleviation of poverty in seriously affected areas.
- (3) Social development and civil society, focusing on university education enhancing regional co-operation, vocational education and training linked to employment generation and civil society strengthening.

The EC intervention in these three main areas needs to be highly focused in order to reach as high an impact as possible and will be provided ensuring synergy and complementarity with Commission's prior and ongoing assistance in the humanitarian field, EU Member States' IFI's and other donors' interventions

### **5.2.1 Support for good governance and institution building**

*Public Administration Reform:* EC assistance in this sector shall primarily concentrate on supporting the preparation and adoption of EC compatible legislation across the administration because the massive legislative approximation and structural reforms necessary in the context of the Stabilisation and Association process will pose very high demands on a public administration which is bureaucratic, over-staffed, poorly trained and poorly remunerated.

The creation of an independent and efficient civil service which provides a decent quality of service to its population whilst operating in a transparent and accountable manner is one of our priorities in FRY. Progress in economic and social reform is dependent upon the building throughout the FRY of efficient, non-political, merit-based public service systems. Reform efforts in this sector need to concentrate on developing systems of accountability, management control and performance based human resource management. The process should also lead to the downsizing and the streamlining of the Public Administration and its de-concentration to municipal level. Public Administration Reforms are difficult to implement and rigorous benchmarking will need to be applied to any EC assistance in this sphere.

Attention will be devoted to help the government to modernise the public administration in the social services and to provide the necessary support to design programmes aiming to alleviate the impact of the economic transition upon the more impoverished layers of the population.

Likewise, support will be provided to the local administrations, via specialised technical assistance and municipal investment funds so that the level of service closest to the citizens is also strengthened.

Due to its high importance and the current poor level, support will be mobilised for the statistical office at Federal level as well as for the Republican statistical offices. This support in form of technical assistance as well as, if necessary, start up equipment, will be closely co-ordinated with European Statistical office.

For Kosovo, assistance will concentrate on supporting the establishment and capacity building of the public service and on the reinforcement of the elected provisional institutions for self-government, so as to facilitate the swift transfer of relevant powers from UNMIK to the new local administration. It is particularly important that rapid steps are taken to introduce the Basic Public Service Law and to put in place the structure of an impartial, politically neutral, public service to take forward the programmes of the new authorities”.

*Justice and Home Affairs:* This is a particularly vital sector for EC intervention in a country whose political class has been linked to organised crime and cronyism. FRY’s overworked and inefficient judicial systems are a great hindrance to the consolidation of a democratic State and the creation of a free market economy. Administrative and legal reform here will also need to help the Government move away from old non transparent systems and procedures by reviewing and streamlining regulations and administrative practices in conformity with EU standards. This must lead to greater transparency, accountability and political neutrality. The courts are spilling over with cases whilst lacking basic IT equipment and being presided by poorly paid and poorly trained judges administrative staff.

The Community will support reform in this area with the following axis in mind: simplification of procedures, training of judges and staff and if necessary investments in equipment for the adequate performance of the tasks. In Kosovo, the judicial system is not only short of qualified judges, and even international judges, but desperately short on judicial physical infrastructure such as police stations, court rooms and prisons.

JHA reforms will have to be supported by a reliable and uncorrupted police and border guard service which is democratically accountable. This too will require a mixture of hard investments but more importantly, intensive training, revised legal frameworks and specialised support to fight terrorist and organised crime. Training to address sensitive issues like respect of ethnic minorities and human rights will be included .

Smuggling and trafficking of human beings and goods has become an increasingly serious problem in the FRY as in the wider region. Tackling all these forms of organised crime, is a major priority which EC assistance will support, not least due to the impact on such crime on the EU itself. Co-operation on the prevention and control of illegal immigration and the development of asylum systems will be fostered. Training of JHA public officials and improved communications systems will be given priority assistance. Standards and methods

for controls on persons and the development of rules concerning visas will also be targeted as well as border control, in close synergy with the activities foreseen in the regional programmes.

*Support to the Customs and Fiscal Administration:* Customs is an area of federal responsibility which urgently needs support both in strengthening capacities and of harmonisation towards the EC. It is a sector which needs an integrated approach as it links in to many other areas of economic and social importance such as justice and home affairs, trade facilitation, taxation and consumer protection. It will need particular assistance via a Federal programme with sub-programmes at entity levels that will take account of the particularities and the different stages of development of the services in each entity. The programme should build on the successful experience of the "Customs Assistance Programme to Kosovo" (CAM-K). Throughout the FRY there is a black economy that remains unregulated and untaxed. A major task is to bring this activity into the main-stream economy so that more funding is available for the provision of public services. It is also essential that efficient systems of direct and indirect taxation are put in place quickly, as trade reforms reduce income from imports. As far as the FRY is concerned, assistance in the customs and fiscal sectors will look at promoting the concept of the single economic space through harmonised tariff and taxation structures, information sharing, cross border co-operation and facilitation of circulation of goods and persons throughout the FRY. Specific attention will be given to the modernisation of legislation and working practises and its approximation to the EU, selection and training of officers, improvement of management skills, introduction of information systems, developing intelligence and best practises to fight against smuggling and organised crime. The modernisation of this service is considered a key objective taking into account that FRY will share a future border of the enlarged EU.

### **5.2.2 Economic reconstruction, regeneration and reform**

EC assistance under this category will focus on laying down the necessary measures to ensure environmentally sustainable economic growth and development. Assistance will be mobilised via the CARDS programme as well as the macro-financial assistance budget line B7-548.

*Macro-Financial support and budgetary sustainability:* The FRY, and in particular Kosovo, is likely to continue to experience budgetary shortfalls and balance of payments problems whilst public expenditure is readjusted, economic restructuring and appropriate levels of revenue raising is properly in place. Over the period of this strategy, exceptional macro-financial assistance is still likely to be needed to support the respective entities during this delicate transition period. The EC macro-financial decided by the Council could support efforts in the context of economic stabilisation and structural adjustment programmes agreed with the WB and the IMF. CARDS assistance will pay special attention to the necessary accompanying measures to ensure better planning and control of federal, republic and entity budgets. This will typically take the form of technical assistance to the relevant financial authorities on financial planning, management of public expenditures, treasury systems, budget classification, revenue collection and tax reforms.

*Investment in key public utilities and infrastructures:* The EC assistance has focused up to now largely on hard investments. These need to be continued, mainly in Kosovo and partially in Serbia, in order to consolidate the Community's interventions made to date. However, Community support for hard investments should be reduced over time as this is an area where involvement of the IFI's is more suitable. EC assistance will continue to support the preparation of such investments but its primary focus will be on institution and capacity building measures which will ensure sustainability of the initial hard investments and allow for European rapprochement in the long term, in particular as regards the involvement of the private sector and the necessary regulatory bodies. It must be noted that such accompanying institution building measures must always accompany hard investments to ensure proper

maintenance and cost recovery systems, without which the initial hard investment is fundamentally flawed.

*Energy:* Some further investments will be required to consolidate the investment undertaken to date to secure power generation, transmission and distribution. Focus on the integration of the FRY in the regional energy market will be essential. Other accompanying measures such as the upgrading and the extension of the coverage of existing heating systems and rationalisation measures may also be necessary to reduce much of the current strain presently experienced by the electric power utilities. Environmental considerations will be taken into account when mobilising support in this area.

In the mid to long term, the Community support will focus on promoting equilibrium between supply and demand at local and regional levels, ensuring that there is a cost effective match between market needs and existing facilities. Community intervention will also help reform the institutional and regulatory framework which lie behind the energy sector in FRY, including billing systems, know how support to possible partial privatisation of the companies and their restructuring and upgraded management skills and techniques as well financial management.

The issues of efficient consumption and poor fee collection rates in the whole of FRY will be particularly urgent to address as important elements in adjusting and rationalising energy supply and demand. Community support could also be directed, hand in hand with the government, to public utilities' education programmes to the whole population, especially as regards rational consumption.

*Transport:* The whole of the federal transport networks need to be rationalised and strengthened, bearing in mind the regional implications within and outside the FRY. The improvement of the safety of the transportation system is also key to trade facilitation and development. Efforts will be concentrated on the development of safety standards taking into consideration the needs of rail, road, navigation and air transport systems according to more rational and multi-modal principles which will in addition have a positive impact on the environment.

Assistance will also be mobilised for the development of a comprehensive strategy in order to deal with the various problems related to border management and trade facilitation. The border crossing points selected to benefit from this assistance will be those which sit on a border with a pre-accession country or either border posts or inland customs clearance points within the FRY territory. Enhanced border management will involve not only strengthening capacities and infrastructures but also, in synergy with assistance programmes in the area of institution strengthening, of border agencies promotion and inter-agency co-operation, customs and border control as well as, if necessary, border demarcation.

Given its unique regional nature, this priority is detailed in the CARDS Regional Strategy and financed with funds from the regional programme. However, measures to address the Integrated Border Management programme will, for reasons of efficiency, be implemented and complemented by the national programmes and for that reason are also described in this Country Strategy Paper.

In the mid to long term, increased attention will be provided to linking the FRY to the Trans European Networks, requiring specialised studies and in certain cases other actions necessary to mobilise governmental and International Financial Institutions funding that will realise the physical connection of FRY to both the transport and energy Trans-European Networks and Pan-European Transport Corridors<sup>7</sup>.

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<sup>7</sup> In particular, Pan-European transport corridors VII and X, and energy networks.

*Environment:* If economic growth is to be sustainable and the quality of life of the local population fundamentally improved, respect for the environment must play a key part of the overall reconstruction and transition process. The main elements necessary in this regard are creating a well functioning legal, policy and institutional framework, strengthening the municipal institutions responsible for solid waste and waste water management, investing in waste management sites and sewerage facilities, helping heavy industry to reduce their emissions and foster regional environmental co-operation.

Industrial pollution affecting the air and soil will need precise monitoring equipment and methodology. This may also involve dealing with 'hot spots' in areas such as Pancevo and Novi Sad whenever industrial damage constitute a threat to public health and eco-systems. Other actors (eg. UNEP) are already active in this area, with some bilateral support.

Environmental audits on parts of the energy and heavy industrial plants should be undertaken with a plan to tackle the worst polluters. Environmental considerations will be included in EC assistance programmes specially in the areas of transport and energy, also aiming to improve public health levels in the FRY .

Assistance in this sector, as with most of the sectors put forward here, will need to strike the right balance in terms of hard investments and technical assistance for institution building measures. Hard investments in conjunction with loans from IFIs may be necessary for a certain period of time in order to alleviate the financial cost for an area which is not ripe for assuming user payment but which gradually will move to this system. As for technical assistance, support will be provided both to the public administration as well a for supporting civil society – including NGOs - which have so fundamentally helped to raise awareness in the recent past on this very important issue.

*Economic development (including rural development):* Community support in this area will help to encourage the growth and reduce the mortality rate of start-up and medium sized enterprises (SMEs), to restructure viable socially owned enterprises (SOEs), to reduce unemployment, to ensure a sound and harmonious regional development and to regain public confidence in the private sector.

As a pre-condition for a well functioning market economy, the Community will contribute to the necessary development of policy and legal frameworks, regulatory institutions, administration reform that are required for a single economic space and that will be based on the Community acquis and fully aligned with the Stabilisation and Association process. The reform of the regulatory framework should help attract domestic and foreign investment and provide the most appropriate environment for the growth of the private sector.

As needs are so substantial due to the many years of mismanagement and directed economy, the Community support will be highly concentrated in the short term on a few critical areas. In this way, an initial support to credit line establishment and to the privatisation and restructuring process of SOEs and Agro-combinats will be followed in the medium term by the substantial participation of private sector investments and the significant involvement of the International Financial Institutions. In the long term, the Community intervention will be limited to areas, which are not normally covered by the private sector, like advice and support to small and micro enterprises, local economic regeneration activities and support for Yugoslav companies to establish partnership with European constituencies.

Special attention will be paid to economically depressed areas heavily affected by the restructuring process, areas with large economic potential or areas with specific regional problems requiring regional solutions where Community expertise can provide an integrated view of support for regional development. Examples of those regional specific areas are the coastal area in Montenegro due to its tourism potential, the industrial depressed areas such as Kragujevac, the agricultural centers in Vojvodina which in addition is hosting a high number

of refugees, and the integrated political economical and civil society developments in Southern Serbia.

The Financial sector requires substantial restructuring all across the FRY and specialised institutions have been established e.g. the Bank Rehabilitation Agency. While recognising the importance of bank restructuring for the functioning of the market economy, this document does not propose any specific intervention in the area. There are more specialised donors and Financial Institutions, like the EBRD and the WB, which are willing and can mobilise resources to support this sector.

On trade development and export promotion the most immediate objective of EC assistance is to ensure that the country is able to fully enjoy the benefits that free access to the EC market can bring and can take full stake of the opportunities that will be arising with the future negotiations of bilateral free trade agreement in the region. In this view, CARDS will support the development of an effective trade-development strategy providing technical and legal assistance to ensure that the partner country's products meet EC's technical and quality standards both in the industrial and agricultural sphere. Particular support will be required for the modernisation of veterinary and phyto-sanitary delivery mechanisms to increase food safety and consumer protection. Assistance will also be provided for the approximation to the Community technical regulations and European standardisation, accreditation and conformity assessment procedures and for fostering the development of the quality control infrastructure. In addition, institutional reforms are necessary for institutions such as the Directorate for Commodity Reserves in Serbia and the State Commodity Reserve Institution in Montenegro to meet the requisites of a free market economy. EC assistance will also be provided to help FRY to prepare for accession to WTO and to the future negotiation of the SAA.

### ***5.2.3 Social Welfare and civil society***

The FRY authorities must address the fiscal costs associated with (and the interdependency between) employment and labour, pensions, education, health, cash benefits and social services. These issues are central to the FRY's pursuit of adopting EU economic and social policy orientations. The main donor lead in this area of reform will be the World Bank which has indicated its intention to provide support to the primary and secondary education levels as well as to the health sector as of 2003. As the EU does not have sufficient resources to cover the full spectrum of these social policy issues, EC assistance will be designed to complement that of the World Bank and other donors through public administration reform programmes to pave the way for them to intervene.

In addition, EC assistance will focus on areas where the Community has a clear comparative advantage so it can make an impact with limited resources. Therefore, EC intervention in the social domain will also focus on university education enhancing regional co-operation, vocational education and training linked to employment generation and civil society strengthening - with special attention to the media sector.

*Education (focused on higher education and vocational education and training):* As in other areas of intervention, the higher education sector needs substantial amount of support. However, due to the limited resources available under CARDS and with a view to maximise synergy with already existing Community programmes, CARDS will focus on a number of realistic and cost effective measures which can impact quickly, such as the participation of FRY University and Research centres in the TEMPUS programme. With a more long-term perspective, a consideration will be given to future actions such as forging twinning programmes with EU universities allowing for fellowships and study visits.

Vocational training in specific sectors will need to be addressed systematically and specially with respect to its complementarity with the proposed activities in the area of economic recovery and growth. Use will be made of the skills available at the EU's European Training Foundation (ETF) for developing strategic plans for upgrading the sector. Whenever possible,

EC assistance programmes will incorporate education and training considerations - notably in the sectors where the bulk of the EC investment is placed. If considered appropriate, EC assistance will act as a catalyst for the creation of vocational training centres. VET activities will focus on promoting the employability of the unemployed or those made redundant.

Employment sustainability and skills development should be a combined effort by the Ministries responsible for Labour, Education, Trade and Industry in close co-operation with employers' organisations and social actors. EC assistance will be necessary to foster strategic planning and frameworks which will help cushion the effects of large-scale down-sizing and will aim to assure workers are trained in the skills required for a reformed economy.

*A functioning civil society:* Building a democratic society based on respect for human rights and the values of equality and pluralism will require the participation of civil society actors, including NGO's and professional associations, and the establishment of an environment which promotes quality public and independent media.

EC intervention will be two-fold. On one hand via the European Initiative for Democracy and Human Rights (EIDHR)<sup>8</sup> - which will devote up to €2 million in the 2002-2004 timeframe to the FRY, it will aim to support democratisation, human rights and confidence building measures between ethnic communities. On the other hand, CARDS assistance will support grassroots initiatives from civil society and professional associations and local authorities targeted to protect citizen's rights and improve socio-economic conditions for the population, with focus on the most deprived and vulnerable.

EC assistance for media will concentrate in the reform of the legal framework for the establishment of independent media, accompanying measures to achieve the financial sustainability of the sector and the transformation of state-run outlets to genuine public service broadcasters. EIDHR will provide complementary support to develop human rights and democratisation aspects of the media sector.

EC assistance will also support the Kosovo Serb community participation in the general public and economic life in Kosovo. Security is however a pre-condition to ensure the sustainability of any action in this field and to provide confidence for the return of the displaced people.

Minority, gender and social vulnerability considerations will be integrated in the mainstream of all EC assistance programmes.

*The return and settlement of refugees, IDPs and its regional implications:* Ongoing socio-political instability is likely to continue due to the high number - and often high geographic concentration - of refugees and displaced persons. This is an issue which will take a substantial number of years to be resolved.

Resolving this issue, whether through return or local integration, will affect local living conditions and will represent additional strains of the delicate situation of the budget accounts. 60% of refugees and displaced persons in the FRY have expressed their desire to integrate while only 6% have indicated a desire to return.

The integration of refugees must avoid the granting of what may be considered a favourable treatment with respect to local population. In this regard, EC assistance programmes will remain focused on socio-economic development benefiting the total population of a region, whatever their ethnic background or status. Areas where there is high concentration of refugees and displaced persons, such as the northern and coastal area in Montenegro and the Vojvodina and Southern Serbia, will receive particular attention.

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<sup>8</sup> Council Regulations (EC) No 975/1999 and No. 976/1999, OJ L120, 8.5.1999 p.1 - 14

The EC will continue to support the policies and guidelines developed under the Refugee Return Task Force and will have regard to the recommendations of the Stability Pact Regional Return Initiative.

#### *Support to the interim administration of Kosovo*<sup>9</sup>

EC assistance will also continue to support the financing of the administrative costs of the “European Union-led” pillar of the United Nations Mission in Kosovo in charge of economic reconstruction and recovery. The EU-led pillar will play a crucial role in associating UNMIK and the provisional institutions of self-government (PISG) to the EU-FRY CTF, to ensure EU-compatibility in policies and measures adopted in Kosovo, and that the specific situation of Kosovo is reflected in SAP activities.

### **5.3 Coherence**

The EC will take advantage and will make the most of having a unique and common implementing body – the European Agency for Reconstruction – to maximise the impute of the assistance in the whole FRY in order to ensure a coherent approach across and within the sectors.

The Agency and other services of the European Commission will ensure co-ordination and coherence of the assistance programmes implemented under CARDS with *other Community instruments*, be it humanitarian aid, macro-financial support, food security, democracy, and other EC programmes.

The proposed EC assistance for the FRY for the period 2002-2006 takes into account the involvement of the other main Community financial instruments, as follows:

ECHO’s involvement in the FRY to date has focused on basic support to refugees and displaced people (food, hygiene, shelter), special social institutions and vulnerable layers of the population; on health care delivery to refugees, IDPs, minorities and other vulnerable people; and on promotion of durable solutions for these caseloads (repatriation of refugees, self-reliance projects aiming at promotion the social and economic re-insertion of the victims of the conflicts), as well as, in Kosovo mainly, on rehabilitation of houses, schools and health centres. On the basis of the humanitarian situation in FRY and the presence of more long-term oriented structural instruments, ECHO has taken the strategic decision to phase out its involvement in the FRY in a gradual manner, first departing from Kosovo (end 2001), then Montenegro (mid-2002) and finally Serbia (in 2003).

In so far as it is possible, CARDS assistance will take due consideration of ECHO’s past and ongoing programmes, and will provide support to the reform of the social services so they can fill the gaps in the basic social net after ECHO’s and other humanitarian agencies exit. In this context, EC response will focus on the structural reforms necessary for ensuring that social needs are catered for by the relevant Ministries and Institutions as part of their normal social support system... In addition, CARDS technical assistance will help to rationalise social expenditure and to improve budget management. The Food Security Programme, which has had an important role in the price liberalisation in the agricultural sector in Montenegro is now in the process of finalising its involvement in the FRY, thus leaving CARDS assistance to address the special needs in relation to food supplies and security as part of the assistance foreseen to the reform of the Public Administration under which agriculture related Ministries/Institutions should be targeted.

CARDS assistance to civil society and media will be co-ordinated with the European Initiative for Democracy and Human Rights - as explained in section 5.2.3. When the priorities of the CARDS programme contains a cross border co-operation character, complementarity with the

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<sup>9</sup> Council Regulation (EC) No 1080/2000 of 22 May 2000, OJ L 122, 24.5.2000 p.27

INTERREG Programme IIIA and Phare programmes will be ensured to the greatest extent possible. This is particularly the case in the Integrated Border Management. To this end, close co-operation will be developed between the country concerned, the CARDS, INTERREG and the concerned EU Member States and candidate countries, including as appropriate the identification of relevant projects in the priority areas of Multi Annual Indicative Programme and regular reporting of progress.

#### **5.4 Complementarity with EU Member States**

Complementarity of EC assistance programmes funded by CARDS with those of EU MS bilateral programmes is critical in order to ensure maximum impact of EU intervention in the FRY and to avoid duplication of efforts. Co-ordination with EU Member States and other donors in the interest of making the Community assistance cohesive and more efficient and complementary is a formal requirement under Article 11 of the CARDS regulation<sup>10</sup>.

The European Commission and the World Bank have played a leading role in ensuring mobilisation and co-ordination of donors via the organisation of international Donor's Conferences.

The first Donors' Conference for the Federal Republic of Yugoslavia was held on June 29, 2001 in Brussels. It followed a donors' coordination meeting which took place in Brussels on December 2000. This Conference provided a major milestone regarding donor co-ordination and complementarity in between donors to meet the needs of the FRY as expressed in the Economic Recovery and Transition Programme.

The needs of Kosovo have already been addressed in separate Conferences which took place in Brussels on 28 July and 17 November 1999 and a technical meeting of donors in Pristina on February 25-26, 2001 prepared in close collaboration with the United Nations Mission in Kosovo (UNMIK) to respond to the needs identified by the Public Reconstruction and Investment Programme.

*Main areas of EU MS intervention* In FRY, the major EU Member States contributions up to date have been received from Italy with substantial involvement in the areas of social welfare, including supplies and technical assistance, and in the area of private sector development either in form of soft loans or Trust Funds, in conjunction with the EBRD and the World Bank. Germany has also had substantial involvement in the areas of Energy and district heating, including energy imports, local infrastructures, and development and support to the SMEs specially its financing. Greece has been active in the in the areas of education and health energy and transport. France, The Netherlands and Denmark have also had important contributions to the Energy sector. The United Kingdom has contributed to the social sector and specially by providing assistance expertise in the areas of privatisation and banking and aid co-ordination. These interventions are fully coherent with the EC assistance provided to date to the FRY.

The main bilateral donor in Kosovo is Germany, heavily involved in private sector, social, economic and infrastructures. Interventions in the commercial banking sector, public utilities and energy sector are largely undertaken either in co-financing or in close co-operation with the EC funds implemented by the European Agency for Reconstruction. EU Member States interventions (Sweden, Norway, Italy, France, Netherlands, Luxembourg, Spain) in the housing and rural programme covering agriculture and small-scale village infrastructure are also highly complementary. Sweden has also supported notably the railways and district heating in synergy with EC assistance programmes to the Energy and Transport sectors in the province. UK's programme in Kosovo has heavily invested in human capital - with particular focus to increase the capacity of the local population and social welfare. Programmes in the

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<sup>10</sup> Council Regulation (EC) No 2666/2000 of 5.12.00, OJ L 306, p.1

health, customs sectors and in support to the Public broadcaster (RTK) are also complementary with the ones developed by the EC through the EAR. Most of the EU Member States has very active human rights and democracy programmes focused on minorities, youth, gender and combating trafficking of women. In addition, the Danish Agency for development (DANIDA) is also heavily involved in the promotion of environmental programmes and has supported a range of waste disposal and waste management projects complementary to the EC programmes.

In order to follow up the consistency of EC assistance to the FRY and the coherence of future intervention areas, co-ordination takes place regularly at different levels:

- Contacts between the EC delegation and the Heads of Missions in Belgrade.
- Close co-ordination with the Republican Aid Co-ordination Units.
- European Agency for Reconstruction's regular co-ordination meetings with the development agencies present on the ground (in Serbia, Kosovo and Montenegro).
- Close co-ordination with the EU-led pillar of the United Nations Mission in Kosovo.
- At the meetings of the Governing Board of the European Agency for Reconstruction.<sup>11</sup>
- At the meetings of the CARDS Management Committee.<sup>12</sup>

## **5.5 Complementarity with other donors**

### *US*

The US assistance to the FRY has been budgeted under separate headings for Serbia, Montenegro and Kosovo. Since 1999, the support to Serbia amounts to 218 mUS \$ with a substantial increase following the fall of Milosevic. This support has been applied to the areas of democratisation, Public Administration Reform (including local development and support to economic activities) agriculture and energy.

US has also provided a 155m \$ assistance package to Montenegro in the areas of economic restructuring, democracy local government and budget support in the areas of pensions and energy costs.

Assistance to Kosovo, has amounted to 315 mUS\$. These funds have directed to three main areas: (i) Economic recovery and reform - providing technical assistance to private sector development and supporting SME's and micro-lending to agricultural development. (ii) Democracy building through assistance to building an independent media and judiciary system (iii) Community Infrastructure and Services to restore services in local communities. Part of the US effort has been to fund technical advisors to the staffing of the EU-led Pillar of UNMIK in particular in the areas dealing with fiscal and industrial reform.

USAID's strategy over the next three-to-five years for each entity encompasses democracy and governance; community development; and broad economic policy reform and private sector development.

### *Japan*

Assistance from Japan to Serbia has been very important in the area of agriculture and energy. In Kosovo, Japan has channelled most of its support through the main UN agencies and has also provided technical equipment (18 m US\$) to the public broadcasting service (RTK).

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<sup>11</sup> Article 4 of Council Regulation (EC) No 2667/2000, OJ L306, 7.12.2000, p.7

<sup>12</sup> Article 10 of Council Regulation (EC) No 2666/2000, OJ L306, 7.12.2000, p.1

### *Canada*

In Kosovo, Canada is providing assistance to the education and primary health sectors as well as to local democratisation and minority projects. Canada is working with UNICEF in the replacement of school material and with the UN Housing and Property Rights Directorate.

### *Norway*

Has made critical contributions in the FRY specially in the areas of energy and municipal development.

### *International Financial Institutions*

The priorities for IFI's intervention are very much in line with the 'Economic Recovery and Transition Programme (ERTP) jointly prepared by the European Commission and the World Bank in terms of macro-economic stability, stimulating growth, improve social wellbeing and improving governance and institutions.

The World Bank has pursued a two phase assistance strategy in the FRY. Prior to the resumption of lending operations, which require the clearance of arrears to the IBRD, the WB has mobilised financial assistance through a special US\$ 30 million Trust Fund for FRY. Five operations have been signed representing a commitment of the entire US\$ 30 million. The Board of Directors has also approved exceptional temporary IDA eligibility for FRY providing access to up to US \$ 540 million IDA resources over three years.

The EBRD has provided early assistance through support to the drafting of the Serbian Law on Privatisation, and for a major project to re-develop municipal services in Belgrade and has outlined five main areas in which it is focusing its initial support to the FRY as follows: a) Financial sector reform, b) funding and support to privatisation of medium size and large companies, c) infrastructure investments in the public sector, with an early emphasis on power, airport navigation and refurbishment, and railway rehabilitation, d) water supply, district heating and environmental services by loans to local municipalities while encouraging the setting up of a regulatory framework, e) mobilise bilateral technical assistance funding to support sector reforms, which are a prerequisite for increased foreign investments and efficient local financial intermediation. The EBRD has started activities in Kosovo in 2001 so it is yet early to assess results. The bank is looking for opportunities to intervene in the privatisation and liberalisation of the telecommunications sector in the province.

The EIB is mainly targeting its involvement to the areas of Transport infrastructures (roads, railroads, airports, port) as well as support for SMEs.

EC intervention, especially in the areas of public administration reform and of infrastructures and utilities will act as a catalyst for facilitating a more efficient involvement of the IFIs, thus ensuring synergy of the grant- based support of the Community and the lending-based intervention by IFIs. In addition, EC assistance will pave the way for the intervention of the IFIs (in particular the World Bank) and other donors in the social domain by mobilising technical assistance to foster reform of the administration in the social welfare sectors.

The Joint European Commission / World Bank Office for South East Europe has been set up to help donors address the current situation in South East Europe and the macroeconomic needs of the countries.<sup>13</sup> The Joint Office is instrumental for assessing needs, providing information and co-ordinating the mobilisation of the international donor community in the FRY.

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<sup>13</sup> Countries covered in this website include Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, and Romania. Available information is also provided on Kosovo, Montenegro, and Serbia.

To that effect, a website ([www.seerecon.org](http://www.seerecon.org)) has been established to publicise and coordinate donor's assistance in the region.

Annex 1 - (Map of the Federal Republic of Yugoslavia)



**ANNEX 2 (Overview of EC Assistance to FRY )**

<b>FEDERAL REPUBLIC OF YUGOSLAVIA ( Million EUROS)</b>
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EC ASSISTANCE	BENEFICIARY	1998	1999	2000	2001	TOTAL
<b>OBNOVA/ CARDS<sup>1</sup></b>	Rep. of Serbia		8.88 <sup>8</sup>	183.8	210	402.6
	Kosovo	7.5	127	275	320	729.5
	Rep. of Montenegro	5	22.5	20	20	67.5
	<i>Total FRY</i>	<i>12.5</i>	<i>158.3</i>	<i>478.8</i>	<i>550</i>	<i>1199.6</i>

<b>HUMANITARIAN AID<sup>2</sup></b>	Rep. of Serbia	N/A	75.13	50.45	47.8	-
	Kosovo	N/A	111.7	28.84	14	-
	Rep. of Montenegro	N/A	18.57	14	7.5	-
	<i>Total FRY</i>	<i>255.22<sup>9</sup></i>	<i>205.4</i>	<i>93.29</i>	<i>69.3</i>	<i>623.21</i>

<b>MACRO- FINANCIAL<sup>3</sup></b>	Rep. of Serbia				N/A	-
	Kosovo			35	30	65
	Rep. of Montenegro			20	N/A	-
	<i>Total FRY</i>			<i>55</i>	<i>375</i>	<i>430</i>

<b>DEMOCRACY/ HUMAN RIGHTS<sup>4</sup></b>	Rep. of Serbia	7	N/A			-
	Kosovo	0.48	N/A			-
	Rep. of Montenegro	1.54	2.2			3.74
	<i>Total FRY</i>	<i>9.02<sup>10</sup></i>	<i>11.64<sup>11</sup></i>			<i>20.66</i>

<b>FOOD SECURITY<sup>5</sup></b>	Rep. of Serbia		10.5			10.5
	Kosovo					
	Rep. of Montenegro		10.4	11		21.4
	<i>Total FRY</i>		<i>20.9</i>	<i>11</i>		<i>31.9</i>

<b>CSFP/UNMIK<sup>6</sup></b>	Kosovo		2	6	11	19
	Rep. of Montenegro	3				3
	<i>Total FRY</i>	<i>3</i>	<i>2</i>	<i>6</i>	<i>11</i>	<i>22</i>

<b>DANUBE CLEARANCE<sup>7</sup></b>	<i>Total FRY</i>			22		<b>22</b>
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<b><i>GRAND TOTAL FRY</i></b>	<i>279.74</i>	<i>398.24</i>	<i>666.09</i>	<i>1005.3</i>	<b><i>2349.37</i></b>
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Note: (N/A) separate allocations not available.

<sup>1</sup> Mostly implemented by the European Agency for Reconstruction

<sup>2</sup> Implemented by the European Commission Humanitarian Office

<sup>3</sup> Implemented by the European Commission - DG ECFIN

<sup>4 5 6 7</sup> Implemented by EuropeAid Cooperation Office (AIDCO)

<sup>8</sup> Programme ran through 2000.

<sup>9</sup> Programme had been running since 1991.

<sup>10</sup> Programme ran through 1999.

<sup>11</sup> Programme had been running since 1994.

ANNEX 3 EC Member States and other donors non-humanitarian assistance to the FRY 1999-2001

Country	Gover & IB			Energy			Transport			Agriculture			Economic dev.			Housing			Environment			Health			Social Development			Other			Total
	K	S	M	K	S	M	K	S	M	K	S	M	K	S	M	K	S	M	K	S	M	K	S	M	K	S	M	K	S	M	
Austria		0,1		0,7	0,7			0,7					2,2	2,0			2,0	2,6		0,4	1,0		0,1	2,6				tbd	15,0		
Belgium													0,9		1,2					0,4			0,2						2,7		
Denmark	10,5	0,8		18,3	3,1					2,4				16,3			8,7	0,4				22,2	4,0	1,0				87,7			
Finland				1,6						1,0				1,0			1,9	1,6		3,2			3,3	2,3				15,9			
France		1,7		0,8	6,3		0,2	0,7		2,1			1,5	1,2	0,8			2,9			0,8	1,6	0,7			7,6		28,8			
Germany	1,5			26,7	65,7		7,3		5,0	7,0			30,0	1,0	45,0			27,8			2,9	12,5						232,4			
Greece		65,6									0,1		17,9				0,4			0,4			0,7					85,1			
Ireland	0,4			0,7											1,0							0,2						2,3			
Italy	0,5	5,8			23,1						0,5		6,5	1,7	0,4			4,5	0,4	1,6	0,7	2,1	6,6			13,0		67,4			
Luxembourg											0,7											0,2						0,9			
Netherlands	8,0			0,0	2,4		10,0			0,1			0,7		1,5				4,3			9,5						36,5			
Portugal																												0,0			
Spain		0,1		0,5	0,6	0,3									0,6							1,1	0,5	0,1				3,8			
Sweden	2,6			13,5	2,2		2,3			4,5			1,2		16,5			0,5		4,0	1,5	4,7	2,7					56,2			
United Kingdom	2,3	0,2	0,2	0,1						0,2			0,8	1,5	1,2	0,4			0,1		2,0	0,4	4,6	14,1		20,6		48,6			
Norway	0,8			3,5	4,6		1,2			1,8	1,8		0,2	0,9	0,2			2,5		0,4		7,9	3,3					29,1			
Switzerland	6,7			13,5	6,7		1,5			3,5			3,0		15,4			15,3			1,2	5,0						71,8			
Canada	9,5			1,5	3,3												0,3		12,9			18,0	0,4					45,9			
Czech				0,9	0,9																							1,7			
Japan				10,0							4,3		3,7		4,2			3,0	19,5			33,0						77,7			
Slovakia					1,3																							1,3			
United States	8,0	9,5		15,0	45,0		0,3		5,7	2,3	60,0	68,0	82,0	0,6			2,0		8,2			74,7	43,0		180,0	9,0	170,0	783,3			
Others	7,4			7,2			2,0				1,0			0,3	22,5			1,0					2,9					44,3			
EBRD					100,0							2,6	69,0															171,6			
EIB								50,0	16,0																			66,0			
World Bank	1,0				6,0		2,4			14,0			8,2	6,0			4,7	2,0	6,2			5,9	10,0			6,0		72,4			
<b>TOTAL (known)</b>	<b>58,2</b>	<b>83,8</b>	<b>0,2</b>	<b>114,4</b>	<b>265,5</b>	<b>0,3</b>	<b>24,8</b>	<b>51,4</b>	<b>26,7</b>	<b>25,7</b>	<b>67,7</b>	<b>119,1</b>	<b>177,7</b>	<b>129,6</b>	<b>69,6</b>	<b>8,3</b>	<b>2,0</b>	<b>56,9</b>	<b>8,9</b>	<b>206,8</b>	<b>83,8</b>	<b>1,1</b>	<b>200,6</b>	<b>35,6</b>	<b>170,0</b>	<b>2048,1</b>					

#### **ANNEX 4 (List of abbreviations used)**

<b>CARDS</b>	Community Assistance for Reconstruction Development and Stabilisation
<b>CSP</b>	Country Strategy Paper
<b>DM</b>	Deutsche Mark
<b>EAR</b>	European Agency for Reconstruction
<b>EBRD</b>	European Bank for Reconstruction and Development
<b>EC</b>	European Community
<b>EIB</b>	European Investment Bank
<b>EPS</b>	Electric Company of Serbia
<b>EPCG</b>	Electric Company of Montenegro
<b>ERTP</b>	Economic Reconstruction and Transition Programme
<b>ETF</b>	European Training Foundation
<b>EU</b>	European Union
<b>FRY</b>	Federal Republic of Yugoslavia
<b>FTA</b>	Free Trade Agreement
<b>GDP</b>	Gross Domestic Product
<b>GNP</b>	Gross National Product
<b>IAC</b>	Interim Administrative Council (Kosovo)
<b>IDPs</b>	Internally Displaced Persons
<b>IFIs</b>	International Financial Institutions
<b>MIP</b>	Multi-annual indicative Programme
<b>JIAS</b>	Joint interim administrative structure (Kosovo)
<b>JRC</b>	Joint Committee on the Return of Kosovo Serbs
<b>KEK</b>	Kosovo Electricity Company
<b>KLA</b>	Kosovo Liberation Army
<b>KTC</b>	Kosovo Transitional Council
<b>NGOs</b>	Non-Governmental Organisations
<b>PISG</b>	Provisional Institutions for Self-government (Kosovo)
<b>SAA</b>	Stabilisation and Association Agreement
<b>SAP</b>	Stabilisation and Association Process
<b>SME</b>	Small and Medium Enterprise
<b>SFRY</b>	Former Socialist Federal Republic of Yugoslavia
<b>SRSG</b>	Special Representative of the Secretary General (of UN)
<b>UNMIK</b>	United Nations Mission in Kosovo
<b>UNSCR</b>	United Nations Security Council Resolution
<b>VAT</b>	Value Added Tax
<b>WTO</b>	World Trade Organisation
<b>YuD</b>	Yugoslav Dinar



ANNEX 5  
**FEDERAL REPUBLIC OF YUGOSLAVIA**  
**MULTI-ANNUAL INDICATIVE PROGRAMME**  
**2002-2004**

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**Information provided:** Each sub-heading above is a priority area for CARDS support.

Within each sub-heading, the following standard information is provided:

- 1) Background
- 2) Objectives
- 3) Expected results
- 4) Programmes to be implemented
- 5) Indicators of achievement
- 6) Cross-cutting issues

- 7) Link to regional strategy (where relevant)
- 8) Conditionalities

## 6 GOOD GOVERNANCE AND INSTITUTION BUILDING

### 6.1 Public Administration Reform

#### *Background*

A poorly run national administration actively hinders a country's development towards becoming a stable democracy and strong market economy. Without a solid institutional framework for the exercise of public power, free and fair elections will not lead to representative or accountable government. Without stable regulatory structures that are favourable to business enterprise and social protection, neither privatisation, nor trade liberalisation nor social welfare will generate sustainable economic growth. A poorly functioning administration harm the FRY's overall momentum in the Stabilisation and Association process.

Strengthening such national institutions is an area where EC assistance can have a special added value - encouraging a rapprochement with EU *acquis* and standards in the FRY, a key task as the FRY moves towards the European mainstream, and pulling on its extensive experience in other regions in strengthening the capacities of institutions.

In Kosovo, public administration reform will depend on support for the establishment of the institutions for provisional self-government which will come into being after the elections in November 2001. EC assistance should focus on ensuring a smooth transition of responsibility to these new local institutions. Provisions of means and know-how will be crucial in allowing these institutions to function effectively and to align legislation and practices with relevant international standards and norms as provided by Article 5.7 of the constitutional framework<sup>14</sup>, as well as allowing them to be associated to the Stabilisation and Association process in the FRY. This will have to be accompanied by capacity-building of civil servants and targeted investments to maximise good governance.

Some sectors of the Public Administration may have to be addressed in a more specific manner. Notable here is the health administration due to its critical importance for the well-being of the population and to its large financial implications on the state budget. Moreover, some limited EC assistance in 2002 for supplies and equipment may be necessary to ensure the consolidation of the investments made to date in the health sector but with the clear view to phasing out and handing over to more specialised donors in this sector. Due account will be taken of the support provided through ECHO programmes in the health sector.

Throughout the FRY, there is a need to decentralise authority from central to local government and, consequently, to prepare local government for undertaking greater levels of responsibility. This movement is problematic because investment in local infrastructure has steadily declined over the last few years, leaving most municipal level public services in a poor state. To help correct this, EC assistance will be provided to enhance the delivery of municipal services.

The implementation and enforcement of public procurement in the FRY remains problematic and a potential source of fraud and corruption. There is a pressing need in FRY to improve public procurement-related legislation and to strengthen the institutional framework and the enforcement of procurement rules. FRY will need to address this issue, given the obligations of a future SAA in terms of alignment of legislation and fair access of EU and foreign firms to public procurement markets.

Another important part of public administration is Statistics. This is a Federal competence - data collation is done at the Republic/Kosovo levels and then processed at federal level (except in

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<sup>14</sup> UNMIK Regulation 2001/9 of 15 May 2001

Kosovo where data is locally processed). The current level of statistical reliability is very poor, reducing accuracy of available information and thus undermining policy formulation. Support from Eurostat shall be provided to help the relevant authorities set the agenda for upgrading this service.

### ***Objectives***

The overall objective is to promote an efficient entity and federal level public administration with a coherent and interconnected body of law that can better meet the demands of a functioning society and of participation in the SAp.

Specific objectives include:

- (1) To support the preparation and adoption of laws and policies compatible with the EU acquis, as foreseen in the Stabilisation and Association process and which are requirements in the Stabilisation and Association Agreements.
- (2) To ensure a more efficient and effective administrative system at federal and republican level, operating more closely to EU best practice.
- (3) To contribute to an efficient and coherent decentralisation of responsibilities to local government levels.
- (4) To promote a more efficient delivery of services from municipal authorities to the local population.
- (5) To ensure the Federation and its constituent entities have access to a reliable source of statistical data and processing.

### ***Expected results***

The proposed assistance will help the FRY to approximate its laws and policies towards the EC acquis and EU best practice. This will help the overall Federation's drive to fulfilling the conditionalities of the SAp.

The support will promote a more effective public administration working within a more sound legal framework that promotes investor confidence and that fosters sustainable economic development taking into account both economic growth and also social concerns.

EC assistance to municipal development will see an improvement in the quality of administration and service being delivered to the local community in the selected municipalities. Training of local civil servants in the running of local government as well investments through a special fund will allow the selected municipalities to tackle serious deficiencies in their local physical and socio-economic system.

An improved statistical service in the FRY will impact on many areas of government and development. It will serve as a more precise "early warning" system for socio-economic problems, such as unemployment and GDP per capita levels, illiteracy. These and other data will give policy-makers the necessary information to put in place the necessary policies and make the necessary budgetary decisions. In addition, EC assistance will ensure the country's effective participation in the Eurostat system.

### ***Programmes to be implemented***

- (1) Technical assistance and capacity building to help administrations approximate policies and legislation with the EU acquis and to improve public service delivery. Special attention will be given to key sectors eg trade liberalisation related reforms, and the ones affecting the well-being of the population particularly. This will include support in the health social and education sectors institutions that will pave the way for the intervention of more specialised donors.

- (2) EC assistance for reform efforts in this sector will concentrate on developing systems of accountability and financial management control at central and local government level, focusing on line Ministries/Departments and relations with municipalities.
- (3) Flexible technical assistance, training and supporting equipment - as appropriate - will be provided to specific agencies that will play a key role coordinating the overall reform of public administration at FRY and Republican levels, for instance Serbia's Public Administration Council, the Agency for Public Administration Development, Montenegro's Ministry of Justice and its Public Administration Institute and the future FRY's European Integration Office and Policy and Legal Advisory Unit.
- (4) EC support in Kosovo's public administration will assist the establishment and effective operation of the institutions for self-provisional government. EC funds will mainly cover technical assistance in the domains of policy definition, law-making processes, audit and training of civil servants. Whenever appropriate, supporting equipment and investment will be provided to lay the minimum prerequisites for the new institutions to fulfil their tasks.
- (5) EC assistance will support a series of pilot projects to certain key municipalities in upgrading their local physical, economic and social infrastructure whilst providing technical assistance to upgrade local officials through on-the-job training, based on EU-style administration and legal frameworks where appropriate.
- (6) The Ministries of Finance and public administration reform bodies will benefit from EC institution building support, training and the associated investment support in order draft and implement new laws and regulations in public procurement procedures. Moreover, a public awareness campaign could be launched at entity level to inform the public and private sector of the new modalities this will implicate.
- (7) On the basis of an agreed federal model, upgrading the Statistics technical infrastructure, including the necessary equipment and corresponding know how and organisation for electronic data transfer and modern statistical techniques.

The instruments for the above programmes will include not only traditional technical assistance and supporting supply programmes but also twinning projects involving the placement of EU civil servants in administrations to help on core activities.

#### ***Indicators of achievement***

- (1) EU compatible laws and regulatory frameworks drafted, passed and enforced, in line with agreements reached with the EC under the SAp (including now the Consultative Task Force).
- (2) Quantity and quality of services delivered by beneficiary municipalities.
- (3) Approval and implementation of public administration reform, including restructuring, training, anti-corruption and performance-related reforms.
- (4) Functioning financial control systems, as measured by audits on revenue and budgeting procedure, public expenditure in beneficiary municipalities and public sector procurement processes.
- (5) Improvement in production and confidence level of statistics, as measured by assessment reports from Eurostat.

#### ***Cross-cutting issues***

- (1) Greater democracy and fairness due to a less politicised and better regulated administration.

- (2) Easing of inter-ethnic tension due to municipalities able to cater for the whole population.
- (3) Policy planning of the administration meets more accurately the needs of the people.

### ***Link to the CARDS Regional Strategy***

The bulk of institution building support from CARDS will be delivered through the national programmes. However, some support for this area is foreseen in the Regional Strategy. However this will help promote cooperation between administrations of different countries and the harmonisation of methodologies across the region in the key areas of institution building and Statistics. Public procurement and audit will also be a priority of the regional assistance. Participation in the General Support Facility which will help promote awareness of the acquis will be a key complementary action to the national programme.

#### ***Programme specific conditionality***

- (1) Progress on drafting, adoption and implementation of laws concerning the reform of the public administration, the functioning of the administration in key areas such as public procurement, budgetary process and financial control and progress on decentralisation and the role of local government.
- (2) Full cooperation with the work of the Consultative Task Force and the future European Integration Office on relevant reforms.
- (3) Transparent civil service recruiting mechanisms introduced and enforced.
- (4) Demonstrated and tangible cooperation in Statistics amongst the entities and between the entities and the federal level at all times and adequate co-ordination with the statistical regional programme.

## **6.2 Justice and Home Affairs**

### ***Background***

Respect for the rule of law and a functioning Justice and Home Affairs policy lie at the heart of a country's capacity to deliver security, justice and freedom to its citizens. Without it - and the strong institutions to enforce it - there is little prospect that a state will either provide effective protection of basic rights or tackle international crime and corruption.

FRY has problems in this area ranging from minority rights through economic development to organised crime. However, recent years are leading to major advances in this area which are clearly recognised.

First, partiality of JHA institutions undermine the respect of minorities, issues that need to be dramatically enhanced to meet EU expectations.

Second, current JHA problems undermine FRY's efforts at economic development. Corruption, lack of enforcement and a backlog of court cases undermines economic development, deters foreign investors and produces frustration and social unrest. In this way, the framework of high legal, professional and ethical standards that an effective JHA policy produces is key to the good functioning of the market economy.

As in other countries of the region, the FRY is confronted with a major problem of organised crime. Substantial smuggling and trafficking of human beings and goods (tobacco to illegal arms sales, drug trafficking, etc.) generate huge sums for criminal groups, terrorists and other extremists and is to the fundamental detriment of the population and a direct challenge to the State. Money-laundering saps economic development and bears heavy social costs too.

Organised crime infiltrates financial institutions, acquires control of large sectors of the economy and offers bribes to public officials. In countries in transition to democratic systems, this criminal influence can severely undermine the process of change.

Of clear priority in this regard is an effective and comprehensive anti-corruption and anti-money laundering policies. This is particularly the case in FRY given that it has no passed and implemented law as yet on money laundering.

As regards Kosovo, decades of existing under a parallel system - whereby most local Kosovars of Albanian origin organised their lives outside the normal parameters of public administration and the judicial system - have undermined the rule of law in the Province. These problems have been exacerbated by the 1999 conflict, the problems UNMIK have had in filling the judicial vacuum left by an absent administration, ongoing political and military tension in the region and continued ethnic tension which is only barely controlled by a heavy military presence under NATO. The KLA has been disbanded with many ex-combatants now participating in the civil emergency preparedness organisation under KFOR's supervision. However, assistance here needs strict and enforceable conditionalities.

As a result of an inadequate police and judicial infrastructure and human resources, the last two years have seen an eruption in crime levels, driven partly by ethnic but also economic problems. The newly established Kosovo police force which is under UNMIK Police's supervision should play a significant role in the improvement of law and order. Therefore, EC assistance will aim at facilitating the proper functioning of this service. Proper police stations and law courts are noticeably few and far between, often leading to make-shift detention arrangements in available buildings. Proper prisons are also inadequate compared to the number of detainees. The capacities of judicial staff will need to be reinforced so as to arrive at an adequately functioning judicial system.

### ***Objectives***

The overall objective is to promote effective justice and home affairs policies and structures that enable the state to guarantee a space of freedom, security and justice for all its citizens.

The specific objectives are to assist the relevant authorities:

- (1) To adopt EU Member States' standards and best practices in the field of JHA- in line with SAp requirements.
- (2) To strengthen the rule of law and ensure its proper enforcement with particular attention to anti-corruption measures.
- (3) To improve the overall efficiency and capacity building of the judicial, prosecution and policing system in the fight against organised crime, including money laundering.
- (4) To strengthen institutional capacities to develop and implement an asylum and migration policy.
- (5) To foster inter-entity and regional cooperation in relation to matters affecting security, including terrorism.

### ***Expected results***

EC assistance will help the FRY authorities strengthen their JHA capacity nationally but also to promote their cooperation with neighbouring countries and policies which are harmonious with those of the EU. This assistance will help result in a normalisation of relations with neighbours and internally between regions.

The overall results which this assistance will help produce will be strengthened capacities in the justice, prosecutor and police agencies and more coherent and feasible policies on minority rights' protection, illegal emigration, anti-corruption and the fight against organised crime. The indicators of achievement below indicate the scale of the ambition that the country has set itself and which the assistance will help to realise. However, this is clearly a long term issue that will go beyond the time scales of this MIP.

CARDS support will ensure the development of an integrated border management strategy covering customs, JHA and other related border issues which will be coordinated with other SAP countries, as well as other implicated countries (eg. EU member states and candidate countries).

***Programmes to be implemented***

*Judiciary and court reforms:*

- (1) Technical assistance will be provided to improve the drafting of laws and regulations in line with EU standards and best practice. This technical assistance should cover methods and procedures for drafting laws, their monitoring and verification, as well as the co-ordination with Parliament, Government etc. The assistance will be given to line ministries in line with their concrete needs.
- (2) EC support to the judiciary will be for the education and training of staff of the Ministries/Courts of Justice. The intervention will assist in curricula review and design and in training-of-trainers' programmes, familiarisation with EU Member States' standards and best practice in justice and home affairs.
- (3) Support will be given to improvement of court and case management, in new legal areas such as economic and commercial law, money laundering and IT-crime etc, as well as laws preventing corruption and abuse of the public administration involving both individuals and companies.

### Policing:

- (1) EC support will be given for the education and training of staff of the Ministries/Departments of Interior. This will be delivered through assistance to curricula development, training-of-trainers and pilot training courses, and will have two foci:

The first focus will be professional policing capacity. In addition to more traditional police skills, CARDS assistance will be given to training for tasks, skills and issues related to: inter-alia (a) new approaches to policing (including community policing and problem oriented policing); (b) police management, accountability and policing ethics; (c) intelligence-led policing, including information technology systems; (d) inter-agency co-operation (eg. procedures for co-operation, different modes of operation and related sensitivity); (e) problem-solving, conflict resolution and negotiation; and, (f) prevention of criminality and methods of technical criminal investigation.

The second focus will be to make the police system familiar with EU Member States standards and best practices in relevant fields, in particular related to SAp obligations linked to justice and home affairs. This will cover in particular the movement of goods and workers as well as international police co-operation.

### Asylum and Migration

To manage the phenomenon of increased irregular migration, FRY would need to be supported in augmenting its asylum systems and migration management capacities. This is an ambitious but necessary approach that has clear national policy implications. Objectives will be to develop and implement a national strategy in this context supported by sectoral and inter-agency work plans.

EC assistance will focus on asylum and immigration legislation alignment with international Conventions and penal legislation on trafficking and smuggling in human beings in conformity with the 2000 UN. Palermo Convention, also a visa regime consistent with EU. Support to enabling increased regional co-operation on asylum and migration will also be given.

### Combating organised crime and corruption:

Combating organised crime and corruption involves both the police and justice areas, and so is dealt with here under a separate heading. However, the programmes to tackle it will be integrated, recognising that only such an approach will ensure the cross-agency coordinated attack that will have an impact on reducing these two problems.

Support will promote first and foremost the inter-agency cooperation between involved justice and home affairs institutions inside the federation and with the wider region that will be needed to fight organised crime. In particular, under EC assistance, there will be a number of co-ordinated interventions to assist: inter-alia (a) Drafting of legislation; (b) Surveillance training; (c) Support to develop intelligence analysis and intelligence operations; (d) advice on witness protection and on informants and undercover operations; (e) new practices in criminal procedures and criminal codes involving, among others, a wide range of economic crime and terrorist activities.

CARDS support will help develop action plans, review legal and regulatory frameworks and strengthen administrative and operational arrangements for drugs trafficking, smuggling, money laundering and terrorist activities.

### ***Indicators of achievement***

- (1) Reduction in the backlog of cases and of the length of time before cases come to trial.

- (2) Improvements in policing and prosecution system using EU standard measures of performance (eg. number of successful cases and convictions).
- (3) Changed culture and mission of police – and measures of successful implementation - towards a decentralised, indiscriminate and publicly accountable force based on the concept of "policing for the community"
- (4) Number of positive evaluations from training courses provided to the staff of Ministries, police and departments of Justice.
- (5) Specific laws – with indicators of enforcement – against organised crime and corruption.
- (6) Implementation of legislation on Asylum and immigration, that approximates towards that of the EU and Schengen in particular.
- (7) Existence of an integrated border management strategy covering customs, JHA and other related border issues which will be coordinated with other SAP countries and EU.
- (8) Establishment of legal frameworks and organisational arrangements to co-operate in relation to matters affecting security including terrorism

***Cross-cutting issues***

- (1) Higher confidence in the FRY legal judiciary and police system leading to higher investments and socio-economic stability
- (2) Greater respect for human and minority rights
- (3) Greater opportunities for refugee returns due to better security prospects
- (4) Greater chance for regional stability by combating organised crime
- (5) Possibility provided for better regional cooperation in order to tackle mutual problems

### ***Link to the CARDS Regional Strategy***

As noted above, border control programmes are part of a CARDS integrated border management approach. This addresses at the border not only border security but also trade facilitation (ie. border crossings programmes identified above). Funds to cover these actions under this strategy have been transferred from the CARDS regional envelope, given the major regional implications of such work. Precise programmes are being developed within an integrated border management strategy for FRY. This strategy will give coherence and greater impact to the various actions foreseen in this MIP on border management involving JHA (border control) as outlined above in this section but also to the transport (feeder roads), economic development (veterinary and phyto-sanitary support) customs (border crossing points) actions outlined in sections 1.3 , 2.2 and 2.4 below.

The strategy will cover not only infrastructure and supplies but also institution building and technical assistance activities to promote inter-agency co-operation. It will be co-ordinated with neighbouring countries given the obvious regional implications (eg. agreement on priority border crossings). This last aspect will be assured through meetings and studies financed through the CARDS regional programme.

The programme will be co-ordinated with the EC cross-border cooperation (CBC) programmes with the accession candidates and INTERREG programmes in the EU member states in the manner outlined in 5.3 of the Country Strategy Paper.

In addition, CARDS Regional Programme will complement these border and other national JHA actions by promoting regional cooperation on JHA matters, especially on international cooperation between national police forces, judiciary and immigration authorities to be more effective in the fight against regional and national organised crime.

### ***Programme specific conditionality***

- (1) The relevant federal and entity Ministries/Departments will introduce and monitor control measures and safeguards to sustain the process in a transparent manner in line with the Stabilisation and Association process.
- (2) The relevant federal and entity Ministries/Departments will continue their efforts to work out a scheme for appropriate remuneration of its police and judicial service in the framework of the Government's Public Administration Reform Programme. The Ministries/Departments will continue their efforts to reduce the turnover of personnel
- (3) The entities will demonstrate visible and tangible cooperation amongst themselves and with the federal level whilst undertaking the necessary reforms and in their daily work
- (4) A proper maintenance and service of the equipment already provided or to be provided needs to be done and demonstrated
- (5) In parallel with the international assistance programmes the Government will gradually allocate more money from the national budget to sustain the progress from its own resources

## **6.3 Customs and Taxation**

### ***Background***

Under the Constitution, customs are an area of Federal responsibility but actual operation is often being more led at the republican level. The Montenegrin authorities have established a separate customs service with different laws that pay revenues collected straight into their own republican level budget. Furthermore, Kosovo's revenue base had to be created virtually from scratch, which explains the need - with the support of the EC assistance (CAM-K) - to establish

an interim UNMIK customs administration in Kosovo which collects the much needed revenue for the Kosovo Consolidated Budget.

This service has been dislocated, regardless of the final shape of the Federal competencies, and is in dire need of co-ordination and harmonisation at Federal level which is then complemented with assistance at the Republic/entity levels.

Beyond this issue of federal and republic competence, customs also needs an integrated approach in terms of its linkages to other areas of government - it has a key taxation role and links directly to justice and home affairs, cross border and trade facilitation and even to consumer and environment protection.

EC assistance will look at promoting the concept of the single economic space among the entities, including trade facilitation, through a harmonised tariff and modernised customs legislation and working practises, information sharing and co-operation on ensuring free move of goods, services, capital and workers throughout the FRY.

Specific equipment and training will also be provided to share intelligence, fight against smuggling and organised crime. Inter-agency co-operation at border and inland customs clearance points with economic operators, transport and customs agents, border police and phyto-sanitary and veterinary control services will also be integral part of the programmes.

In the context of the integrated border management, border crossings selected for strengthening an improvement must not only be national priorities but also must reflect the priorities of Trans-European Network corridors and the potential for fostering trade facilitation with SAp country neighbours.

Internal FRY customs clearance depots will facilitate a controlled transit of goods between the Republics/entity and the EC Customs assistance programmes in the FRY will ensure the cohesive management of customs throughout the territory.

The administration of the taxation services in the Federal Republic of Yugoslavia is the responsibility of the Republican Governments, and thus prior to the crisis there were two Public Revenue Departments – one based in Belgrade for the Republic of Serbia, the other based in Podgorica for the Republic of Montenegro. There is now a third taxation service in Kosovo which is part of UNMIK and under the management of the Central Fiscal Authority. Like customs, these three services have received different levels of assistance from the international donor community and have begun to develop along different paths and at different speeds.

In order to ensure the cohesive management of customs taxation throughout the territory, it is necessary to begin a comprehensive programme of modernisation and development in Serbia and Montenegro and, through the CAM-K programme, to support the process already begun in Kosovo by UNMIK. Coordination to the extent possible is necessary to ensure business and private persons' can operate effectively between different parts of the federation.

### ***Objectives***

The overall objective is to promote a modern and efficient customs system on processing, inspection and revenue collection that permits the operation of a single economic space within FRY and that facilitates trade regionally with SAp neighbouring countries, candidate countries and the EU.

The specific objectives are to assist the relevant authorities:

- (1) To modernise the customs and taxation services at Federal/Republican and Kosovo levels so as to bring it closer to EU working practises and international standards.
- (2) To foster the free circulation of goods and people within the territory.
- (3) To rationalise revenue raising potential, including the fight against tax evasion.

(4) To produce reliable data to monitor trade flows and to fight against fraud.

***Expected results***

An efficient and effective Customs and taxation service will generate greater revenue for the budget, facilitate trade through faster processing of goods vehicles, foster confidence building between citizens and economic operators and act as a solid deterrent to organised crime.

EC assistance in this sector will enable policies, customs and tax regimes to be established in line with EU norms and Community acquis and will strengthen institutional capacities of agencies involved, extending the work of EC assistance missions such as in Bosnia-Herzegovina (CAFAO) and continuing the one already established in Kosovo (CAM-K). Lastly, EC support will help strengthen border transiting facilities and procedures, including support not only to infrastructure but procedures for processing and inter-agency cooperation with border guard agencies.

CARDS support will ensure the development of an integrated border management strategy covering customs, JHA and other related border issues which will be coordinated with other SAP countries, as well as other implicated countries (eg. EU member states and candidate countries).

### ***Programmes to be implemented***

In order to support the customs and taxation services service meet their reform and upgrading objectives, EC assistance will be mobilised to:

- (1) Draft EU compatible legislation and train officers in implementing procedures.
- (2) Introduce modern management procedures for staffing and organisation.
- (3) Support the reinforcement control and management of transit, including at both border crossing points and in-land customs clearance facilities. This will imply introducing systems to improve processing of trucks, spot checks, computerised exchanges of data between checkpoints and across borders, a reliable guarantee system, and the capacity to use transit data for the automated preparation of inland clearance declarations
- (4) Develop a valuation control system and improve control of origin of goods. This will involve the expanding use of “post-release checks”, requiring the introduction of administrative capacity to follow-up on evaluations and queries, investigate specific customs’ cases, training, and co-operating with other administrations.
- (5) Improve intelligence and enforcement providing support in terms of training, equipment and legislative adjustments providing Customs with greater powers of investigation and prosecution.

### ***Indicators of achievement***

- (1) Increased performance of the customs and tax departments, in terms of processing time at clearance terminals and across international and internal borders, in capacity to monitor traffic flows and in greater efficiency and effectiveness in revenue collection.
- (2) An increased co-operation amongst the different services with the FRY and with other equivalent services in the region, leading to an harmonisation of tariff structures and customs procedures.
- (3) A reported reduction in levels of corruption, smuggling and illegal trafficking.
- (4) Existence of an integrated border management strategy covering customs, JHA and other related border issues which will be coordinated with other SAp countries and EU.

### ***Cross-cutting issues***

- (1) Trade will be facilitated due to the improvement of customs and taxation procedures leading to regional stability and generation of wealth.
- (2) Customs work will complement FRY’s justice and home affairs reforms by acting as a front line barrier against international and organised crime and combat illegal immigration.
- (3) Better inter-ethnic relations created through greater co-operation and collaboration due to improved circulation of goods and people.

### ***Link to the CARDS Regional Strategy***

Customs work above will be complemented with a strategy which will be financed through transfers of funds from the Regional CARDS programme, under the heading of Integrated Border Management. This will give coherence and greater impact to the various actions foreseen in this MIP not only on customs but also JHA (border control) and transport (feeder roads). See 1.2 for further detail.

The above programmes will include where relevant actions that promote FRY's obligations to create a free trade area within the region.

***Programme specific conditionality***

- (1) Demonstrated and tangible cooperation amongst the entities and between the entities and the federal level. Over time, customs must cooperate increasingly with neighbouring SAp and candidate countries.
- (2) Signing necessary international and other agreements to permit cross border cooperation on trade matters.
- (3) Full participation by FRY to deliver on its promise to create a free trade area within the region.
- (4) Access to information and inter-agency cooperation necessary for the efficient implementation of the programme.
- (5) Code of conducts for staff and transparency for recruitment and appointments.
- (6) Guarantees on security of international staff deployed.

**7 ECONOMIC RECONSTRUCTION, REGENERATION AND REFORM**

**7.1 Energy**

***Background***

The stabilisation of energy supply is a basic pre-requisite to the overall economic reconstruction process and to the welfare of the general population of the FRY.

Kosovo and Serbia have suffered many years of neglect and lack of investment in this area, problems which have been compounded by recent conflict damage. Despite significant funds from the EC and other donors to help overhaul large parts of the energy generation and distribution infrastructure, the energy issue remains severe.

Montenegro's energy problems are no less critical – again they are characterised by long-term under-investment and a large industry base that pays unsustainable low energy prices. The inevitable result is an existing infrastructure which operates below capacity and a demand which exceeds supply by 30 %. This deficit is addressed by importing electricity from other interconnected grids, including from Serbia.

The main energy source in the three entities is coal mining, mainly used as fuel for the nearby power plants but also partly for district heating facilities. Any policy analysis of the generation possibilities in the FRY will have to take into account this special characteristic.

Significant capital investments will still be required for generation, transmission and distribution in order to stabilise the domestic supply of electricity in Kosovo. This will include linking Kosovo to the FRY and wider Balkan grid. In parallel, the KEK company will need to be transformed into a competent and sustainable utility company, a task requiring substantial technical assistance and equipment to modernise financial, technical and administrative management. The restructuring of KEK's ownership is a difficult but necessary step to attracting major investments outside the donor community. Assistance will also be needed on the demand side to promote a more rational pattern of energy consumption.

In Montenegro and in Serbia, there is also the need for investment to optimise existing energy generation and distribution infrastructure. Major investments needs in production and distribution utilities will be financed with IFI involvement. This however needs to be facilitated by an adequate energy sector strategy. The institutional capacity and the policy making and regulatory aspects of the sector – involving government, utility company and municipal authority

levels - need to be addressed as a matter of priority in order to ensure appropriate restructuring of the sector.

Across the FRY, energy prices need to be set at appropriate levels more in line with adequate pricing systems. This must focus on billing and payment systems, ensuring that both industrial and household users pay for what the energy they use. This will help place a true economic cost on energy and so reduce wastage and promote a better balance between supply and demand.

The generation and distribution infrastructure needs to go through major repairs and rehabilitation programmes in order to ensure adequate levels of supply. Following appropriate policy decisions, the sector restructuring and privatisation needs to be addressed, clearly addressing the issues of generation, transmission and distribution, with a solid participation of the private sector .

As a horizontal matter, special attention will have to be given to the rationalisation of the inter-entity exchange of electricity in the context of the wider import and export arrangements in the region as well as environmental considerations

### ***Objectives***

The overall objective is to to enhance the policy of the energy sector that feasibly promotes better balance of supply and demand, reconnects distribution networks and addresses wastage throughout the sector.

The specific objectives are to assist the relevant authorities:

- (1) To strengthen the institutional capacities at ministry level.
- (2) To restructure the relevant state owned companies (KEK, EPCG and EPS), so they may eventually run as commercially viable and transparent organisations, and to align with the Community orientations on electricity market liberalisation.
- (3) To ensure adequate pricing tariffs on energy units which are in line with EU best practices to cover the running costs of the sector.
- (4) To rationalise energy exchange to and from other parts of the FRY and with the wider region, including consistency with the trans European energy network connection strategy.
- (5) To attempt to decrease the demand made on electricity production.

### ***Expected results***

This programme will see this essential public utility stabilised and secured in the near term whilst laying the foundation of a restructuring which should allow the utility to function in a sustainable and autonomous manner in the longer term.

This programme will consolidate the investments the EC and other donors have made in the sector to date.

Based on these actions, KEK EPCG and EPS will be en route to becoming financially and operationally viable companies run with greater transparency and competence whilst the users will be properly metered and billed, will be wary of wastage and will likely be more inclined to search for alternative fuel sources. This will largely depend on finding a solution to many of the outstanding political and legal constraints, particularly in Kosovo, which has hindered any outside investment to date.

### ***Programmes to be implemented***

In order for the energy sector to be able to deliver an adequate service to the population, the following EC assistance will be provided:

- (1) Further investments in power generation, transmission and distribution to finalise and consolidate investments undertaken to date by the EC (in particular in Kosovo) and to facilitate the loans financed by the International Financial Institutions. This may involve the procurement of works and spare parts.
- (2) Technical assistance for institutional support, in particular to Kosovo's UNMIK Public Utilities Department and its successor entities and to the - to be created - Energy Efficiency Departments.
- (3) Technical assistance to help central administration and involved companies put in place an appropriate tariffication and billing policy and to help rationalise consumption.
- (4) Financial and operational audit of KEK, EPCG and EPS (of both the fixed and moveable assets) in preparation for a restructuring of the companies and possible part privatisation.
- (5) Technical assistance to the relevant authorities to rationalise the import and export of energy to and from neighbouring countries and electricity exchange between the entities, including help on developing agreements for intra-regional connections.
- (6) Provision of training, which in some cases could be in form of twinning, to relevant government officials, management and operational staff working in KEK, EPCG and EPS.

#### ***Indicators of achievement***

- (1) A strategy for the sector whose implementation will ensure a more balanced supply and demand at entity, federal and regional level.
- (2) Regional agreements in place for energy imports/exports signed up by end of 2002.
- (3) Adequate tariffication policies in place by 2003 and an increase of revenue collected from the utility users.
- (4) Average amount of kilowatts per consumer per day aligned with better consumption practices.
- (5) An assessment of the utility companies' financial situation and restructuring / privatisation plans drawn up for the sector by the end of 2002 and Plans for privatisation underway by beginning of 2003

#### ***Cross-cutting issues***

- (1) Higher standard of living due to the availability of more reliable energy supply.
- (2) Fewer health problems due to the better heating and less pollution.
- (3) Less strain on the central budget for subsidising energy allowing for more expenditure in the social sectors.
- (4) Improved regional and inter-entity relations through energy import/export - and exchange arrangements.
- (5) An environmentally sound energy policy, taking into consideration environmental impact of the foreseen investments.

#### ***Programme specific conditionality***

- (1) Political commitment to restructuring the energy sector, including necessary cooperation from all authorities and utilities to work on restructuring.
- (2) Entities demonstrating visible and tangible cooperation amongst themselves in the planning and implementation of energy related investments as well as in establishing agreements for energy exchange within the FRY and the wider region.

- (3) Judicial and enforcing procedures are established for “bad payers” and illegal connections to the power grid.
- (4) Sufficient publicity/information campaigns are up and running to inform the public of the problems of wastage
- (5) Cooperation from the utility companies is shown during the auditing process and implementation of restructuring plans.

## **7.2 Transport**

### ***Background***

The availability of a functioning transport system will be the key to sustainable economic growth of the South East European region. Without adequate transport systems linking the countries together and the region to its neighbours, trade cannot flourish and the most obvious physical means of achieving closer association with the EU will not be realised. The FRY is crossed by two European corridors which will be key in achieving the transport targets for the country.

There are a number of clear problems that assistance must help address. There is a lack of developed motorway networks and expressways. This problem is compounded because almost all main roads have open access, creating conflict among individual types of traffic and between the traffic and the local road environment. Maintenance and repair have been underfunded due to constrained public budgets.

The transport administration while suitable some years ago now needs major overhaul, especially as regards basing decision on economic rather than political motivations and strengthening the capacity of transport management on issues like budgeting and adequate preventive maintenance.

Current problems on intermodality and overall transport networks limit the flow of people and goods across borders and thus constrain FRY's and indeed the region's economic future. National and CARDS regional funds will be used to ensure cooperation and networking between the national agencies involved in the area and to undertake the necessary investments, especially at border crossing points.

EC assistance in this sector will be provided in close coordination with the EBRD, EIB and the World Bank Transport and Trade Facilitation Programme for South East Europe and with the EC assistance programmes to the Customs administrations. In addition, cooperation and coordination with INTERREG programmes may help promote cross border connectivity with transport infrastructure on the candidate or member state sides' of the FRY borders. Environmental considerations will be taken into account when mobilising EC assistance in this sector

### ***Objectives***

The overall objective is to facilitate the flows of goods and people internally to the FRY and externally to the wider region.

The specific objectives are to assist the relevant authorities:

- (1) To strengthen transport related infrastructure on border crossings to facilitate trade flows with the neighbouring countries.
- (2) To facilitate the loan activities International Financing Institutions (IFIs) for their loan investments through the preparation of feasibility studies, technical designs and occasional co-financing.
- (3) To help ensure that adequate and EU approximated policy and legal frameworks are in place in the domains which include among others inspections, safety standards, taxation and works quality control.
- (4) To strengthen transport authorities' capacities on policy making, budgeting, infrastructure planning and implementation.

### ***Expected results***

EC assistance will help strengthen the transport linkages between the entities of the Federation, regardless of evolutions on the political front. This in itself is a significant contribution to the wider region as trade and movement of people are immeasurably facilitated through better border and in-county transport infrastructure. Moreover, investment and tourism will be encouraged thus boosting the economy.

The programmes proposed will help facilitate the strategic planning and financing of key elements of the transport network in terms of trade facilitation and utilisation. Support for infrastructure investments may be provided but the overall approach is to facilitate a lead role for the IFIs where large and long term physical investments are required.

EC assistance will help develop critical transport routes within the framework of getting FRY linked to the Trans-European Network (TEN) corridors VII and X. Concretely, CARDS support will ensure that all border crossings on the TENs through the FRY will be completed to an appropriate standard by 2006.

The particular added value of EC assistance will be the institutional strengthening aspects whereby the Transport Ministries and their sub-bodies will be able to plan the sector better, ensure EU best practice maintenance and safety standards and allow the sector to be minimally subsidised through significant revenue raising from the users.

### ***Programmes to be implemented***

In terms of upgrading transport conditions and institutional arrangements, EC funds will be used in the following manner:

- (1) EC assistance in this sector will mainly focus in providing technical designs and feasibility studies in order to allow the financing of investments from IFIs. EC funds will only be used to invest in hard infrastructure on border crossings within integrated border management (prioritising TENs crossing points) where there is either a strategic priority (e.g. Sloboda bridge in Novi Sad), and on exceptional cases, when there needs to be co-financing or which cannot be funded through a loan arrangement. Priority sections will be those which favour Yugoslavia's links to the TENs (especially corridors VII, and X) and within the Federation.
- (2) EC technical assistance will be provided to the transport regulatory bodies as there is an urgent need to ensure their sound development by building institutional capacity to

improve budgeting, prioritise investment needs, prepare and manage construction projects, prepare an asset database and formulate a planned maintenance system.

- (3) In Kosovo, due to the difficulty IFIs currently have in operating there, CARDS assistance will continue, bringing the transport infrastructure to reasonable levels to allow for economic development. Specific activities for institutional capacity building will be required to ensure the sustainability of all investments here. Particular focus will be given to the transport access linking Kosovo to the rest of the FRY and to targeted infrastructure essential for municipal development.

***Indicators of achievement***

- (1) Improved trade flow figures, including access, at border crossing points, prioritising those on TENs corridors.
- (2) Average transit times and costs for travelling within the FRY.
- (3) Investments performed by the IFI and complementarity achieved.
- (4) Alignment to EU legislation and best practices specially in what respects adequate maintenance of the infrastructure, safety and taxation.
- (5) A decreased amount of accidents registered and its health and economic consequences.
- (6) More accurate budgetary planning and implementation by the relevant authorities, both on new infrastructure and maintenance.

***Cross-cutting issues***

- (1) Improved inter-ethnic relations through stronger trade links and increased contact between peoples.
- (2) A boosted economy due to increased trade and economic activity.
- (3) A reduced mortality and injury rate as well as less health expenditures due to safer transport usage.
- (4) An environmentally sound transport policy, taking into consideration environmental impact of the foreseen infrastructures.

### ***Link to the CARDS Regional Strategy***

In the border regions, regional transport facilitation will be promoted through CARDS support to integrated border management. This addresses at the border not only trade facilitation (ie. border crossings programmes identified above) but also JHA issues of border security. Funds to cover these actions under this strategy have been transferred from the CARDS regional envelope, given the major regional implications of such work. Precise programmes are being developed within an integrated border management strategy for FRY that is being funded using 2001 funds. The programme will be co-ordinated with the Phare cross-border cooperation (CBC) actions in the accession candidates and INTERREG programmes in the EU member states in the manner outlined in 5.3 of the Country Strategy Paper.

### ***Programme specific conditionality***

- (1) The FRY agrees to priority border crossings with neighbouring countries, as set down in an integrated border management strategy.
- (2) The FRY and entity governments are working closely with the IFIs and make particular efforts to mobilise their involvement, finance and take responsibility for the investments made.
- (3) The entities demonstrate visible and tangible cooperation amongst themselves and with the federal level in the planning and implementation of transport infrastructure investments.
- (4) Institutional reforms will take place inside the relevant Ministries/Departments which will allow better planning and maintenance of road transport facilities.

## **7.3 Environment**

### ***Background***

If economic growth is to be sustainable and the quality of life of the local population fundamentally improved, respect for the environment must play a key part in the overall reconstruction and transition process within the FRY.

To this end, an environmentally aware approach will be used inside all EC assistance programmes. In addition, dedicated CARDS support projects will be financed that address environmental concerns notably in the waste and waste sectors.

In terms of water and waste water management, Kosovo and Montenegro are the entities which have been the most seriously affected by widespread water shortages and inadequate treatment and disposal of used waters.

In Kosovo, ongoing projects initiated through EC funds must be completed involving technical assistance, works and equipment to ensure water supply in urban and rural areas is improved. Thereafter the EC will phase out of such investments and, as in transport and energy, focus on a more facilitating role for national and IFI actions, noting that such major investment work should be led by IFIs. Concretely therefore EC will finance, including but not only in the waste water treatment and disposal area, feasibility studies and technical designs with some possible limited co-financing alongside the IFIs, where absolutely necessary.

Until the break up of the SFRY, Yugoslavia had shown itself to be quite progressive and environmentally aware compared to its neighbours, strongly influenced by civil society groups active in the sector. However, a sharp increase in energy intensity per unit of GDP, a wider use of low quality fuels and more harmful emissions from the energy and heavy metal industry have now brought about high levels of urban and air pollution. On another front, water sources fell to unsatisfactory quality levels with the increasing amount of poorly run municipal and industrial waste sites, ad hoc fly-tipping created particular problems in the coastal and larger cities as

regards groundwater quality. The recent conflict has also left its environmental scars with toxic losses from damaged industries and public concerns raised by the possible health consequences of the armament used.

FRY's participation in the activities of the European Environment Agency will also be promoted through EC assistance.

### ***Objectives***

The overall objective is to protect the citizens of FRY from health risks linked to toxic pollution of air, water and soil while ensuring future economic development is environmentally sustainable.

The specific objectives are to assist the relevant authorities:

- (1) To plan for a more systematic and efficient solution to environmental concerns, with the treating of solid waste and waste water as the most immediate priorities.
- (2) To approximate environmental norms to those of the EU.
- (3) To facilitate investments in this area, linked to a coherent and feasible environmental strategy for the FRY.
- (4) To facilitate FRY's participation in international environmental networks, notably the European Environment Agency, and to promote civil society involvement on environmental issues.

### ***Expected results***

EC assistance to this sector will help the FRY combat some of its most serious environmental problems in a more practical and strategic manner, particularly the highly toxic, industrially created environmental problems. This will result not in greater protection of the population's health in high risk zones.

Local authorities will be properly equipped and have a sufficient knowledge base with which to face up to these problems.

Regulatory frameworks will be introduced, keeping industrial and other pollution policies in line with EU norms.

In terms of solid waste and used waters management and disposal, EC assistance will provide support to planning, institutional capacity and reforms necessary for the provision of an adequate, systematic and cost-effective service. It will be based on supporting the restructuring of the present utility companies and the introduction of sufficient financial cost recovery mechanisms from the users of the utility. Coupled with limited essential investments in works and equipment (and facilitating the activities of leading IFI's), EC assistance will help waste to be managed more effectively and in a manner which is in line with EU best practices.

### ***Programmes to be implemented***

- (1) Technical assistance to central authorities in order to draft, adopt and implement new environmental policies and laws.
- (2) Technical assistance for strengthening the central and municipal institutions' capacities to deal with water supply, solid waste and waste water management problems.
- (3) Technical assistance and exceptional procurement of equipment for pollution monitoring.
- (4) Limited infrastructure programmes to remediate heavily polluted sites which have direct health implications and threaten bio-diversity. This may involve: (a) dealing with 'hot spots' in areas such as Trepca, Pancevo and Novi Sad; (b) equipment and vehicles may

be exceptionally financed which collect and dispose of solid waste in chosen municipalities, with close regard to regional development initiatives in these areas; (c) completion of the hard investments made to date in the Kosovo water supply system and waste sector.

- (5) For waste water management, EC assistance will act more as a catalyst for investment from national and IFI sources. This will include an initial evaluation of the existing sewerage and treatment facilities and feasibility studies on specific corrective projects. Due to the absence of tradition for paying for these type of services, some initial and limited co-financing alongside the IFIs and the municipalities themselves may be provided.
- (6) Environmental audits will be undertaken according to usual Community assistance programmes, when addressing, investment in infrastructures or in the energy sector
- (7) Support to the maintenance and further development of a civil society network, which have played such an important role in the environmental sector in the past.

#### ***Indicators of achievement***

- (1) Legislation passed that reinforces and makes sustainable FRY environmental policies.
- (2) Number of penalties against environmentally harmful activities by companies and other measures of compliance.
- (3) Improvement of public health indexes linked to environmental pollution.
- (4) Increased monitoring and more accurate reporting on environmental emissions, including on industrial chimneys, water sources and soil samples near to industrial activity.
- (5) Amount of waste processed in municipal disposal sites and amount of revenue generated by the municipalities from this public utility.
- (6) Level of civil society activity in the environment sector.

#### ***Cross-cutting issues***

- (1) Fewer health problems caused by pollution.
- (2) Positive effect in other areas of economic development such as tourism and agriculture.
- (3) A civil society conscious of all the problems affecting society including awareness on environmental issues.

#### ***Programme specific conditionality***

- (1) Environmental legislation developed in line with EU standards
- (2) A system for appropriately penalising industries and individuals who pollute beyond acceptable international norms
- (3) Governmental environmental action plans drafted up per entity by the end of 2002

### **7.4 Economic development**

#### ***Background***

In a country impoverished by years of conflict, sanctions and economic mismanagement, the priority must now be to establish the basis for sound economic growth. A decade of political isolation has also led to FRY companies tending to focus purely on local markets and partnerships.

In order to overcome these obstacles particular efforts will be required to put in place regulatory and legislative frameworks conducive to the development of enterprises, the establishment of a

well functioning financial sector, the modernisation of the trade and fiscal regimes as well as support for creating regional and EU based business links.

An overhaul of the present economic legislation and financial regulatory environment is a basic precondition to provide a reliable environment for companies to develop and for attracting investment. Attention to property rights and ownership rights will be of fundamental importance to create confidence for investors. The SAP provides a useful framework for FRY to modernise its legislation and make it compatible to EU acquis.

On trade, the main objective is for FRY to fully enjoy the potential of benefits that entail expanded trade relations at regional and international levels. In this respect, the autonomous trade measures<sup>15</sup> granted by the EU already opened up a window of opportunity for FRY.

Against this background, it will be necessary to support the FRY as follows: a) assist at preparatory stage FRY's current negotiations for Free Trade Agreements with partner countries in the region to secure consistence among them and with the SAAs ; b) assistance for FRY's integration in the multilateral trading system, being FRY's accession to the WTO a priority; c) strengthen FRY's capacity in a number of regulatory areas such as standardisation and conformity assessment, trade defence measures, trade related intellectual and industrial property rights, services, etc d) targeted assistance to institutional reforms, such as helping the commodity reserves and veterinary and phyto-sanitary control departments, to meet the requisites of a free market economy.

The SOEs include most substantial enterprises in the FRY. SOEs have to operate as viable companies but cannot do so without a clear insight into their assets and liabilities, especially important in attracting outside investors. To this end, preparatory work on audits and restructuring plans are vital. This support can lead to conversion into joint stock companies, spin offs or restructuring of large companies.

Another strategic focus is the promotion of Small and Medium Enterprises (SMEs) which make a vital contribution to the dynamism and flexibility in all sectors of FRY's economy and help underpin the development of a free market economy, a key development in achieving closer association with the EU. SMEs will have to play an important role in employment generation and will help alleviate social pressures which will result from the restructuring of SOEs.

Although the EC is presently providing financing programmes (grant co-finance) for SMEs initiatives, it will in future focus more on improving the business climate for SMEs and on institution building that supports the development of businesses and private enterprise. Special attention will still have to be given to the highly rural based economy, especially in Kosovo.

Support on economic development must also recognise the needs to address the needs of the significant refugee and displaced population in the FRY (as mentioned in the CSP). Focused assistance will be mobilised to help those refugees and internally displaced persons who do not wish to return, such as in starting business and retraining. The same attention needs to be directed to the very impoverished areas and sectors of the FRY in order to avoid uneven economic development and social instability. Due account will be taken of the support provided through ECHO programmes to these populations and of the experience gained in the sector. Any EC involvement to tackle this problem will have to be closely coordinated with the World Bank poverty assessment exercise.

To conclude, special attention will be provided to sectors of the economy or geographical areas with special economic potential or hardships, so that the Community intervention contributes to a long lasting economic recovery.

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<sup>15</sup> Council Regulation (EC) No 2007/2000 of 18.9.00, OJ L 240, 23.9.00, p.1 and (EC) Council Regulation (EC) No 2563/2000 of 20.11.00, OJ L 295, 23.11.00, p.1

### ***Objectives***

The overall objective is to reinforce the country's recovery and to promote its sustainable economic development.

The specific objectives are to assist the relevant federal and entity authorities:

- (1) To underpin the sustainable economic development of the FRY, including the creation of a single economic space, compliance with SAp obligations, especially as regards the internal market, and the integration of the FRY in the international trading system (including WTO membership).
- (2) To help improve the ability of FRY producers to trade and collaborate with the EU and regional partners, including the creation of local and international business partnerships.
- (3) To support the development of SMEs, the restructuring and privatisation of the public sector and stimulating development in sectors or areas of high economic potential.
- (4) Strengthen the municipalities ability for designing and implementing local development initiatives.
- (5) Provide focussed support to areas of high refugee population and/or areas of high levels of poverty.

### ***Expected results***

EC assistance to the sector will help the country to realise its restructuring policies on economic development and to bring its laws, policies and regulatory institutions into line with the Community acquis.

After a decade of isolation, EC support in this sector will also help the country become more closely linked into the regional and world economy. Specifically, EC support will help the FRY to realise its promises to open its doors to the external market as well as to benefit from a preferential trade regime with the EU and bilateral agreements with its neighbours. This will do much to boost the economy, even if certain non-restructured industries will initially suffer from the gradual abandoning of protectionism and the introduction of price liberalisation.

Support on internal market related areas will result in an increase in the number of EC standards adopted, higher level of protection of intellectual and industrial property, greater vet and phyto-sanitary controls, establishment of structures to perform conformity assessment procedures and gradual implementation of a market surveillance system.

Although initial reforms may lead to higher unemployment levels, this is expected to be more than compensated for by the creation of new enterprises or the expansion of existing ones. However, to ameliorate impact of such restructuring, EC support will help the authorities implement specific mechanisms for regional poverty alleviation and refugee support.

### ***Programmes to be implemented***

- (1) Technical assistance in order to draft, adopt and implement a well functioning legal, policy and institutional framework for a soundly based market economy.
- (2) Provision of technical assistance for addressing regional trade negotiations and WTO accession requirements.
- (3) Design and implementation of the institutional and organisational requirements for an agricultural, veterinary and industrial certification, inspection and quality control. These will involve equipment, specific technical assistance and training. All programmes will comprise institution building and training support for the main bodies involved in the accreditation, certification and market surveillance process (eg. national standards body, future accreditation bodies, certification bodies, associated laboratories). Investment support will be provided to ensure these structures gradually obtain the technical means to carry out their tasks.
- (4) Technical assistance will be needed in order to raise the profile of the reformed institutions and strengthen their role as catalysts for the promotion of SMEs.
- (5) Support will be provided to FRY companies' participation in EC-backed entrepreneurial events and to support agencies for SME promotion in sectors of high development potential. In exceptional cases, support may be provided to pilot test financial support instruments addressing the specific needs of SMEs.
- (6) Targeted support will be provided in the context of the Privatisation and restructuring of companies, to facilitate this process. This will take the form of assistance for technical and financial audits and the preparation of business plans
- (7) On regional development, the Community will focus its efforts on a limited number of geographical areas with particular socio-economic problems or high development potential. This could be the case of industrially depressed areas, regions with high concentration of refugees and displaced population, the Presevo valley or the northern and coastal area in Montenegro. It will catalyse instruments such as credit lines, vocational education and training and SME assistance at local level, including grassroots initiatives.

### ***Indicators of achievement***

- (1) Enforcement of new policies and laws for the functioning of a single economic space, in line with EU internal market approaches.
- (6) Progress on readiness to capitalise on EU trade agreements, conclusion of regional trade agreements and implement WTO requirements.
- (7) A functioning accreditation, certification and market surveillance system, as shown by reports on the capacity of industrial veterinary and agricultural products to meet quality and safety standards of the Internal Market.
- (8) Number of SME start-ups and survival rates, and the number of agreements and partnership established with EU companies.

### ***Cross-cutting issues***

- (1) Improved international relations due to increased economic ties and closer economic ties with the EU through increased business links
- (9) Better health safety due to more stringent agricultural veterinary and industrial produce controls
- (10) Better inter-ethnic relations due to a greater focus on trade and business exchanges

- (11) Higher standards of living for the vulnerable population of FRY due to targeted income generating assistance

***Link to the CARDS Regional Strategy***

Complementary measures on trade facilitation (financed under the CARDS regional programme but implemented through this CARDS national MIP) within the CARDS integrated border management approach are covered above in the sections on customs, transport and JHA.

***Programme specific conditionality***

- (1) Political commitment to market economy principles, trade and price liberalisation
- (12) The FRY and entity governments working closely on trade issues and facilitate the principle of a single economic space.
- (13) Commitment to re-enforcing the institutions working on private sector development.
- (14) Support and close co-operation with institutions dealing with approximation to EU legislation.
- (15) Political commitment and negotiations on facilitating the return of refugees to their country of origin

## **8 SOCIAL DEVELOPMENT AND CIVIL SOCIETY**

### **8.1 University education, Vocational Education and Training and Human resource development**

#### ***Background***

Education has recently suffered from budgetary cut backs leading to a lack of investment, and to an overstaffed but under-paid work force, poor buildings and obsolete facilities. The overall organisation of the system needs to be reviewed in order to close facilities which are under-used and re-enforce the ones which are currently working on multiple shifts.

Primary and secondary education are also important when looking to support the entire system, but the EC will concentrate its limited resources efforts on two key areas where it has a comparative advantage and greatest potential impact:

- (1) Support to the University education via the participation within Community programmes in the area of education (TEMPUS), promoting higher education reform and its impact to economic development and the strengthening of civic society.
- (2) Assistance to Vocational Education and Training (VET). Vocational Education and Training builds on the expertise and programmes of the European Training Foundation (ETF).

For vocational training, an assessment will need to be made on what facilities already exist and in what sectors. If considered appropriate, EC assistance will act as a catalyst for the creation of vocational training centres, under the guidance of ETF.

#### ***Objectives***

- (1) To improve higher education by supporting FRY universities' participation in collaborative activities via the TEMPUS programme. These activities would lead the way for the introduction of new structures of governance and management as well as for the decentralisation of the Higher education system. They would also support the promotion of curriculum reform in key disciplines, in line with the objectives of the Bologna Process (creation of a European space of higher education), of regional co-operation in South-East Europe, student and staff mobility as well as networking activities.
- (2) To ensure that higher education and vocational training joins mainstream employment and human capital developments in the region and wider Europe.
- (3) To enhance education authorities and social partners capacities in the provision of education and training that meets the demands of the labour market.
- (4) To support the modernisation of the vocational education and training system for both youth and adults and adapt it to needs of the labour market

### ***Expected results***

EC assistance will help the sector gear education and training towards employment at a time when unemployment is already high and enterprise restructuring is likely to initially aggravate the problem.

Harmonisation with EU best practice in the sector in general and in the area of VET, especially by means of contacts established with equivalent European institutions, is also expected to be a key result of this programme.

EC activities will result in increasing numbers of students, unemployed and redundant workers entering the VET systems or university exchange programmes, either to deepen a skills base or to re-orientate existing skills and qualifications. The involvement and awareness of local authorities in the importance of this sector will be reflected through their reinforcement of the institutions that will support these measures.

EC assistance, through the TEMPUS Programme will foster higher education reform and the integration into the developing European space of higher education.

### ***Programmes to be implemented***

EC assistance will support the development and implementation of a coherent vocational education and training policy in order to deal with the requirements of the economic restructuring process and minimise negative social impacts.

Programmes will include supporting the participation of FRY universities into the Community Tempus programme.

Other training and education related programmes will include:

*Preserving and generating jobs at the local and national level by:*

- (1) Enhancing the institutional capacity of local authorities to develop comprehensive employment training strategies on a cross-sectoral basis.
- (2) Training to strengthen the skills' base of the employed (including managers, staff of firms and entrepreneurs) in sectors that have economic potential for development so as to enhance their competitiveness.
- (3) Support local partnerships and local employment initiatives

*Assisting the unemployed and the redundant through:*

- (1) The improvement of employment services and the enlargement of their scope on issues such as job/social counselling, job search/job clubs programmes, labour exchange and placement services, relocation services.
- (2) The retraining of the unemployed for increasing their employability

*Better preparing young people to enter the labour market through:*

- (1) The modernisation of the vocational education and training system for young people so as to inculcate attitudes, skills and knowledge that correspond to the requirements of a changing labour market

### ***Indicators of achievement***

- (1) Key decision-makers aware of the European dimension in higher education and VET
- (2) Number of TEMPUS projects in which FRY has participated, including the number of partnerships established and students exchanged with European education establishments.
- (3) Participation rates in VET programmes, including data on re-employment and employability on a sector and regional basis.
- (4) More active participation of the social partners to the issue of human resources development.

### ***Cross-cutting issues***

- (1) Participation in TEMPUS will enhance regional co-operation
- (2) Less inter-ethnic and social tension due to greater fairness of opportunities as regards education and the labour market;
- (3) Better opportunities for women to access higher level and better paid jobs
- (4) Greater possible mobility of the population around the Federation and the region leading to better international relations
- (5) Closer ties to the EU as education and VET policy is aligned to EU norms and links are created with academic institutions of the EU
- (6) Economic regeneration is rendered more sustainable by the advent of a continuous source of young professionals
- (7) Improved access to labour market for people with special needs;
- (8) Access to labour market is provided to ethnic minorities on a more equal basis

### ***Programme specific conditionality***

- (1) Commitment to ensure fair access to education and training for both genders and all ethnic minorities
- (2) Commitment to reforming the curricula and teacher training in higher education and vocational training, in the context of the complete reform of the education system
- (3) The policy for human resources development is recognised as a top priority by the institutions and made part of the Governments' policies for economic and social cohesion.

## **8.2 Support to civil society (including independent media)**

### ***Background***

In a new and fragile democracy such as can be found in the FRY, where links to the overthrown Milosevic regime still exist and where past governmental control over the media has been extreme, measures need to be rapidly undertaken to consolidate the new democratic processes.

Scarred by the last decade and the recent conflict, inter-ethnic relations and confidence building between communities are poor. Extremist views on different ethnic groups are still wide-spread, egged along by frequently biased media reports, particularly in Kosovo. Moreover, regional turbulence has produced significant numbers of refugees and Internally Displaced Persons (IDPs) for whom the quality of life, security conditions and integration is low.

In Kosovo, in particular, the role of women in society is often limited by the cultural and post-conflict factors. These women (particularly in rural zones) are then ill equipped to play a revenue raising role as they are sometimes left to their own devices.

In FRY, there is a need for community driven development which is directly related to capacity building of selected local NGOs and civil society groups to allow them being more effective and increase the impact of their actions, to improve their image within local communities and to achieve higher participation of citizens, especially young people, so that they can express and lobby for their rights and better work together on issues of socio-economic concerns.

Another important area that needs developing is the building of partnerships between local governments, business and non-profit sectors. There ought to be a linking of private, civil and public sectors at local level with an aim at contributing to local community empowerment and social inclusion, economic development and increasing democratic control and accountability.

The support to the media sector should focus as much on a structural reform as on a targeted support to media operators. This includes several major fields of intervention: reforming the media and public information legal frameworks, supporting the transformation of state-controlled media, and converting state-run TV from political mouthpiece to genuine public service broadcaster, as well as promoting a sound private

### ***Objectives***

- (1) To ensure the creation of a suitable legal and administrative environment for the establishment and functioning of local non-governmental organisations, lobby groups, professional associations and establish mechanisms for its interaction and partnership with the authorities.
- (2) To support the consolidation of democratic principles within local authorities and to promote confidence building, return or integration.
- (3) To facilitate public participation in the governmental decision making process, including civil society initiatives with socio-economic impact.
- (4) To facilitate a better provision of accurate information by the public broadcast services and independent media, including a healthy co-existence of public broadcasters and independent media.

### ***Expected results***

In terms of grass roots organisations, required to support, economic development and social protection, EC support will seek to address their often weak financial capacity and inner management skills. One will expect to see increased evidence of local organisations (such as NGOs, civil society and professional associations, etc) monitoring and supporting the work of central and municipal government, in building partnerships between local governments, business

and non-profit sectors, in facilitating a consultative process in the running of the administration through advocacy and lobbying activities and last, but not least, ensuring that gender and minority issues are impressed upon the policy and law making processes.

Through EC support to the sector, Media (be it written or televised) will have its quality raised and its journalists better trained in order to give a reasonably accurate account of national and international events in a comprehensive, clear and independent manner. In Serbia and Montenegro, where there is already a certain quality and diversity of journalistic opinion is, EC assistance will need to place a lot of emphasis on addressing management issues and financial solvability. In Kosovo, greater hand-holding will be necessary.

#### ***Programmes to be implemented***

- (1) Technical assistance for helping the FRY governments to develop a legal and institutional framework supporting the existence and participation of the civil society actors and NGOs.
- (2) Support local actors aiming to increase interest and debate on sustainable social and economic development, assisting the most vulnerable and the development of deprived areas.
- (3) Support in Kosovo through technical assistance the establishment of a Public Broadcast service.
- (4) Support to independent media that moves from covering survival needs to a market oriented approach aimed at bringing selected, quality media operators to their financial sustainability.

#### ***Indicators of achievement***

- (1) Quality of legislation establishing the legal framework for civil society and independent media operators.
- (2) Quantity of local NGOs/local, associations and independent media registered
- (3) Number of projects developed by NGOs/local associations
- (4) Number of active confidence building measures initiated
- (5) Reports from human rights and civil society organisations.

#### ***Cross-cutting issues***

- (1) Greater transparency and sensitivity in the running of central and local public administration due to a more profound respect of public opinion and the notion of serving the people
- (2) Better inter-ethnic relations due a better social debate and provision of information
- (3) Better regional relations and relations with the EU and the international community
- (4) Improved women participation in the society
- (5) Better accountability of the government initiatives
- (6) A more environmental and social conscious economic development, accountable to the population.

#### ***Link to the CARDS Regional Strategy***

CARDS regional support will also be provided to complement the above national programme activities by focusing on democratic stabilisation projects involving international organisations and partnerships between organisations in FRY and other countries. The Democracy Programme

will also have activities in the FRY and will focus on more democratic and human rights issues than the CARDS national programme.

***Programme specific conditionality***

- (1) Drafting and implementation of a new law governing NGOs and local associations
- (2) Establishment by the authorities of platforms aimed at encouraging the development of civil society.

Annex (MIP-Indicative Allocation of resources)

Multi-Annual Indicative Programme				FRY			Kosovo			Montenegro		
				Serbia (*)								
Sectors			FRY	2002	2003	2004	2002	2003	2004	2002	2003	2004
<b>Governance&amp;Inst. Building</b>												
Justice & Home Affairs			35-47	3,0	9-13	7-12	7,0	3-5	3-4		3,0	
Customs & Taxation			21,5-27,5	5,0	4-6	4-6	2,5	2-3	1-2	1,0	1,0	1,0
Public Admin Reform (1)			90,2-110,2	15,0	25-30	20-27	13,7	5-10	5-8	2,0		4,5
of which statistics			4,5	2,0	1,0		1,0					0,5
<b>Eco Reconst. Regen&amp;Reform</b>												
Energy			233,6-271,6	67,0	50-70	40-50	55,0	10-15	7-10	2,6	2,0	
Transport			84,7-107,7	44,0	20-33	10-20	6,0			2,2		2,5
Environment			35,2-45,2	0,5	10-13	10-14	5,0	3-5	1-2	1,7	4,0	
Economic development (2)			136,5-166,5	21,0	45-55	30-40	19,0	10-15	5-10	3,0	1,5	2,0
<i>Housing</i>			16,0	-----	-----	-----	16,0	-----	-----	-----	-----	-----
<b>Social and Civil Society</b>												
Education & VET (3)			37,5-46,5	2,0	12-15	12-15	4,5	3-5	2-3			2,0
Tempus programme			16,5	4,0	4,0	4,0	1,0	1,0	1,0	0,5	0,5	0,5
Civil Society and NGOs			19,3-22,8	3,5	5-7	4,0	4,3	1-2	0,5-1		1,0	
<b>Other</b>												
Agency's administrative costs			50-56	10,0	10-12	8-10	9,0	5-6	4-5	2,0	1,0	1,0
Specialised assistance & studies			21,9-23,9	3,0	6,0	6,0	2,9	1-2	1-2		1,0	1,0
Transfer UNMIK			8,0				8,0					
<b>Up to total (4)</b>			<b>904,9</b>	<b>180,00</b>	<b>240,00</b>	<b>195,00</b>	<b>154,90</b>	<b>50,0</b>	<b>40,0</b>	<b>15,00</b>	<b>15,0</b>	<b>15,0</b>
Integrated Border Management *			<b>28,2</b>		See below		See below				See below	

(\*) These figures include the support to Federal wide activities

(1) Including assistance to social welfare sectors (e.g. Health) (2) including agriculture (3) including employment generation measures (4) as per budget available, maximum range in a sector is compensated by lower amounts, within the indicated range, in other sectors.

<b>Integrated Border Management</b>	(From CARDS regional programme)	<b>2002</b>	<b>2003</b>	<b>2004</b>
		<b>9,7</b>	<b>10,0</b>	<b>8,5</b>