

ANNEX

COUNCIL REPORT - Review of the Stabilisation and Association Process

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I. Introduction

The Stabilisation and Association Process represents the European Union's commitment to contribute to peace, democracy and prosperity in South-Eastern Europe. In line with the General Affairs Council's decision of 9 April 2001(1) to undertake annual reviews of the countries of the Stabilisation and Association process, and the decision to conduct an early, political review already in June 2001, the Council has prepared an assessment of each country in the context of the strategic objectives of the Stabilisation and Association process. The first part of this report explains the overall rationale behind the Stabilisation and Association process, its objectives and how it can allow the EU to help each country achieve sustainable reforms and to move closer to the overall goal of EU membership. This part is followed by a summary of country assessments, which contains recommendations for further action to be taken by the countries concerned, and operational conclusions relating to: Albania, Bosnia and Herzegovina, Croatia, the Former Yugoslav Republic of Macedonia and the Federal Republic of Yugoslavia.

II. From Regional Approach to the Stabilisation and Association process

After a period of violent conflict in the region the EU Regional Approach of 1997(2) sought to underpin the implementation of the Dayton/Paris and Erdut agreements and bring basic stability and prosperity to the region. In June 1999 the EU(3) set out a more ambitious vision for the region's development. This was based on:

- a recognition that the main motivator for reform in these countries is a credible prospect of potential membership once the relevant conditions have been met(4), as offered at the Feira European Council. It clearly goes beyond the former offer of "contractual relations" (Trade and Co-operation Agreements) in the Regional Approach;
- the need for the countries concerned to establish normal mutual relations, which would allow greater economic and political stability in the region to develop;
- the need for a more flexible approach enabling each country to move ahead at its own pace.

This flexibility is balanced by a common set of political and economic conditions so as to maintain the integrity of the EU's overall policy towards the region(5).

In July 1999 the Stability Pact, which also contributes to the core aims of the Stabilisation and Association process, was launched.

III. The Stabilisation and Association process (SAP)

The Stabilisation and Association process is a long-term commitment to the region in terms of both political effort and financial and human resources. The process represents an overall framework in which preferential trade concessions, an assistance programme and a new contractual relationship should assist each country to progress, at its own pace, and on the basis of the implementation of necessary reforms, on the way towards the prospect of EU accession.

The 24 November Zagreb Summit set the seal on the Stabilisation and Association process by gaining the region's agreement to its objectives and conditions. The Summit stated in particular that "democracy and regional reconciliation and co-operation on the one hand, and the rapprochement of each of these countries with the EU on the other, form a whole". The countries of the region thereby undertook to abide by the EU's conditionality and use the Stabilisation and Association process, and in particular the Stabilisation and Association Agreements when signed, as the means to begin to prepare themselves for the demands of becoming candidates for EU membership some time in the future. Thus conditionality, as a policy addressing the region as a whole, is the cement of the Stabilisation and Association process.

a) Trade

The EU is by far the most important trading partner for the region. The promotion of trade flows is a core action for the EU within the Stabilisation and Association process. The Lisbon European Council of March 2000 stated that Stabilisation and Association Agreements should be preceded by asymmetrical trade liberalisation. Since December 2000(6), the EU has accordingly applied a highly preferential trade regime to all the countries covered by the Stabilisation and Association process. The opening of EU markets to products from the Stabilisation and Association process countries is intended to promote foreign investment, develop export capacities and contribute to the overall political and economic stability of the region. The granting of autonomous, preferential trade measures remains, however, subject to compliance with relevant Stabilisation and Association process conditions, including readiness to engage in effective economic reforms and in regional co-operation.

b) Assistance

EU assistance requires that certain political and economic conditions inherent in the Stabilisation and Association Process be met. CARDS(7) brings a more strategic approach to assistance to the countries concerned. It underpins the objectives and mechanisms of the Stabilisation and Association Process. As each country moves deeper into the process, assistance will focus increasingly on support for the reforms and institution building as required by the Stabilisation and Association Agreements. But this is not to ignore the political requirement of responding to crises, as necessary, and carrying out the massive reconstruction task the Community has been set. The challenge to Community policy is to respond effectively to volatility, while holding a steady course towards the strategic goal of integration into the EU.

c) Stabilisation and Association Agreements

Stabilisation and Association Agreements are a high-value political tool which, much as the Europe Agreements did for other countries, provide the formal mechanisms and agreed benchmarks whereby the EU can work with each country individually to bring it closer to EU standards. The Stabilisation and Association Agreements represent both the cornerstone of the Stabilisation and Association process and a key step towards its completion. The conclusion of Stabilisation and Association Agreements represents the signatories' commitment to complete, over a transitional period, a formal association with the EU. Such association is based on the gradual implementation of a free trade area and on reforms designed to achieve the adoption of EU standards, including enhanced co-operation, notably in the field of justice and home affairs, with the aim of a gradual rapprochement with the EU.

Differences between agreements for individual countries are likely to be reflected principally in the transition period towards full association with the EU and in the precise phasing and articulation of obligations. But the destination for all countries is expected to be the same: the full realisation of an association after a transitional period through implementation of the same core obligations.

- First phase: towards an Agreement

For the countries which are still working towards a Stabilisation and Association Agreement the "Consultative Task Force/High Level Steering Group" approach has proved an effective means of focusing authorities' minds on essential reforms and of engaging with them in a sustained way to secure implementation. The process is both pedagogical and political. It is based on clear objectives for reform, a work plan and a careful political judgement of how fast each interlocutor can realistically make progress.

- Second phase: implementing the Agreements

Effective implementation of the Stabilisation and Association Agreement is necessary for harmonisation with EU standards. The Stabilisation and Association Agreements do not, however, require signatories to endorse the whole of the EU acquis in one go. The focus is rather on respect for key democratic principles and the core elements of the EU acquis, which allow the EU single market to function properly. By extension through a free trade area with the EU and the associated disciplines (competition and state aid rules, intellectual property etc) and benefits (e.g. rights of establishment), this will allow the economies of the region to begin the process of integration into EU structures. For areas where the agreements do not impose specific obligations relating to the EU acquis there are provisions for detailed co-operation with the EU, again the purpose being to help each country to move closer to EU standards.

The Stabilisation and Association Agreements, then, are posited on respect for the conditionality of the Stabilisation and Association process agreed by the Council. But they also bring with them a dynamic means of operationalising that conditionality and give the EU the leverage necessary to get the countries to adopt genuine reforms with a view to achieving the immediate objectives of the agreements. The mechanisms of the Agreements themselves will enable the EU to help prioritise reforms, shape them according to EU models, to address and solve problems, and to monitor implementation.

Signatories to the Stabilisation and Association Agreements should understand that effective implementation of the agreements is a prerequisite for any further assessment by the EU of the country's prospects of accession.

d) The Regional Dimension

The Stabilisation and Association process is not simply a bilateral process with each country. With the democratic changes in Belgrade it has become possible to tackle more common

issues and objectives at a regional level. The Zagreb Summit placed considerable emphasis on the central need for regional co-operation as part of the EU's "contract" with the Stabilisation and Association process countries. Similarly, the Stabilisation and Association Agreements include a clear commitment to regional co-operation. The policy objectives are principally:

- to encourage the countries of the region to behave towards and work with each other in a manner comparable to that of EU Member States. An important means to this end will be the establishment of a network of close contractual relationships (conventions on regional co-operation) between the signatories of Stabilisation and Association Agreements;
- to create a network of compatible bilateral free trade agreements (as part of the conventions mentioned above) which would mean that there were no barriers to movement of goods between the countries of the regions nor between them and the EU and, in effect, neighbouring candidate countries;
- to achieve the gradual re-integration of the countries of the Stabilisation and Association process into the infrastructure networks (TENS) of wider Europe (transport, energy, border management);
- to ensure that the authorities in the countries of the region work together to respond effectively to the common threats which organised crime, drugs trafficking, illegal immigration and other forms of trafficking represent for the region's and the EU's security. In many cases, e.g. on visa policy, a common approach by all the countries will be needed to deal with the threat effectively. In this context, and as a follow-up to the commitments on justice and home affairs made at the Zagreb Summit, the countries of the Stabilisation and Association process have recently signed the Sarajevo Declaration on regional co-operation on asylum and migration.

Each country's contribution to achieving these objectives will help to determine the EU's assessment of that country's implementation of a Stabilisation and Association Agreement. The agreement on succession issues recently reached by the five Successor States of the former SFR of Yugoslavia represents a significant step towards reconciliation and normal neighbourly relations.

The Stability Pact complements the Stabilisation and Association process and will continue to be an important forum on which the Union can draw to further the strategic goal of the Stabilisation and Association process, in particular the dimension of regional co-operation. Constructive co-operation within the Stability Pact will therefore be recognised as a positive effort towards improving regional co-operation.

IV. Objective of the "Review Mechanism"

The range and depth of the new relationships embodied in the Stabilisation and Association process have not reduced the need for certain conditions to apply at all stages. The objectives of the EU's "Review Mechanism" in the Stabilisation and Association process are:

- to be able to regularly assess whether each country's level of compliance with Stabilisation and Association process criteria warrants the current level of engagement with the EU. In the event that this is not the case the Stabilisation and Association Agreements, the Autonomous Trade Measures Regulations and the CARDS Regulation provide for decisions on appropriate action;
- to provide a benchmark against which to judge how well a country is implementing the Stabilisation and Association Agreement;
- to agree on priorities for EU co-operation;

- to provide a tool for decisions on the further development of the relationship with the EU.

V. Country assessments

A) Albania

Domestic politics are dominated by preparations for the upcoming parliamentary elections scheduled for 24 June. Politics remain polarised, and personalities rather than policies still largely dominate the political debate. Despite progress achieved in ensuring public order and tackling criminality, state control in some parts of the country still remains weak. The stability of Albania is also influenced by forces outside the country, in particular by the situation in the ethnic Albanian inhabited territories across its borders and by organised crime. Albania has made great efforts to improve its relations with its neighbours, and has played a constructive role during the latest crises in the region, notably in FYROM and Kosovo.

The economy has been gaining in strength. In 2000, GDP grew by 7.8 % with respect to the previous year, while equal success was reached in the fiscal area, with a 25 % increase in tax revenues with respect to 1999 and a decrease in the fiscal deficit from 11.5% of GDP to 9.5% in 2000. Foreign financing of the deficit was consequently reduced from 6% to 4.5% of GDP.

1. Issues needing special attention

Democratic Principles

Albania's Constitution guarantees democratic freedoms such as political pluralism, freedom of expression and freedom of religion. Following adoption of the Constitution of Albania in November 1998, the authorities are in the process of undertaking major institutional reforms including the legal and judicial system. To this end, a number of new institutions have been and continue to be created, such as the appointment by the Parliament of Albania's first Ombudsman, the adoption of a new Electoral Code, the establishment of a complete Civil Service Commission, the establishment of the State Publication Centre and the School of Magistrates. Nonetheless, Albania needs to improve its performance considerably in the field of implementing democratic principles, as well as in that of institutional capacity, in order to achieve European and Community political standards.

Achieving such standards in practice means further strengthening the principle of separation of powers, by means of suppressing remaining interference between the legislative, executive and judicial organs.

- Completing the legislative framework in all fields and enhancing the capacity of the judiciary.
- Consistently implementing and better monitoring of the Anti-Corruption Plan.
- Holding free and fair elections in accordance with democratic principles, and carrying out outstanding improvements in the electoral process.
- Overcoming the country's confrontational political environment.

Human Rights and Rule of Law

Albania's Constitution guarantees respect for human rights. While the constitutional court ruled out the death penalty as unconstitutional in December 1999, in September 2000 Albania ratified the Convention on the Protection of Human Rights and Fundamental Freedoms and thereby took a further significant step towards European standards. However, implementation of existing rules need to be reinforced. The Council of Europe is currently preparing a report

on the conformity of Albania's legislation and practices with the European Convention on Human Rights.

Civil society remains underdeveloped. It lacks sufficient financial resources as well as advocacy skills and in practice is not yet capable of playing its role in the country. Outside the capital, civil society is hardly present.

Freedom of expression and association is guaranteed in Albanian. However, in practice, the independence of radio and television needs reinforcing and the transformation of the State TV and Radio into an independent broadcasting institution needs to be completed. The opposition continues to breach the Law on Television and Radio, which requires it to participate in the National Council on Radio and Television.

The right of assembly and demonstration is in general respected in keeping with a recently enacted relevant law. However, there have been isolated cases where the treatment by the local authorities of detained persons has not abided by European norms and standards. The right to property is guaranteed in theory, but it needs further clarification and engagement with a view to creating a functioning and contemporary property and land market (cadastre).

Improvement in implementing the rule of law in Albania, along with sustained efforts to combat organised crime, should constitute the country's top priorities since they remain very serious problems, which hamper improvement in many other areas. The poor state of the judiciary, due to lack of qualified human resources, widespread corruption and party affiliation must be targeted for concentration of resources and attention. The poor working conditions, poor state of the Courts and Court Administration and poor performance and co-operation between the local prosecutor's office, the police and the judges needs to be urgently reversed.

- Completing the legal framework for the judiciary, and enhancing the training of judges.
 - Ensuring the proper application of human rights legislation by the judiciary and law enforcement agencies, including by means of improved training.
 - Improving the capacity of and co-operation between law enforcement bodies.
 - Enhancing the fight against organised crime, smuggling and trafficking in human beings.
- Respect for and Protection of Minorities

Albania's Constitution guarantees the rights of persons belonging to national minorities and in general these are respected. The most important minority in Albania is the Greek minority, however, there are also small communities of Slavo-Macedonians, Montenegrins, Vlachs and Roma. The Albanian government is committed to organising during the next few years a census on the ethnic composition of the population as well as to presenting new minority legislation.

The Albanian government has committed itself to further improving the relevant legislation in order to adapt it fully to existing European standards. In September 2000, Albania ratified the Council of Europe Convention on the Protection of National Minorities, but it has not yet proceeded to implement the reporting obligations associated with its ratification. Albania guarantees the right to use minority languages in court proceedings, however, in practice, the costs of translation/interpretation must be paid by the interested party.

The Greek minority in Albania is organised through the association named Omonia and is represented at the political level through the Human Rights Union Party, currently in the ruling coalition. The minority enjoys normal access to the media. Last year's local elections were unfortunately marked by nationalistic overtones and a consequent rise in tension and

irregularities in certain polling stations in the Himara municipality, where a sizeable ethnic Greek minority lives.

- Abolition of "minority zones", with the aim of ensuring the possibility for minorities to exercise effectively all their rights (i.a. property rights, the possibility to obtain education in mother tongue) throughout the country in accordance with Albania's international obligations.
- Drawing up a national strategy for their social and economic integration, namely for the Roma communities.
- Undertaking a census on the ethnic composition of the population in line with international standards.

Market Economy Reform

Continued progress has been made as regards macroeconomic stability as well as in implementing the pre-requisites listed in the Commission's Feasibility Report, despite the persistent structural weakness of the Albanian economy and the high percentage of the shadow economy. An important element expected to contribute to improved public expenditure management has been the adoption by the government at end of 2000 of the Medium-Term Expenditure Framework (MTEF) (2001-3). As for trade liberalisation, Albania became a member of the WTO in 2000 and is on track for fulfilling the commitments undertaken in this context. Indeed, it currently has no quantitative restrictions on imports or exports, and has reduced the maximum tariff rate from 18 to 15% (Jan. 2001). Due to the sizeable shadow economy, statistical data have to be carefully considered.

In the field of privatisation further progress was achieved with the full liquidation, lease or selling of all small and medium-sized enterprises in Albania by the end of 2000. Successful privatisation in June of the Albanian Mobile Communications company paved the way for the concession awarded to the second mobile telecommunications operator in February 2001. During 2001 it is expected that parts of the oil sector (Servcom) will be privatised as well as the copper and chrome mines. Privatisation of the Savings Bank is also expected to be completed by the end of 2001. The law on the privatisation of between 51 and 76 % of the fixed net operator "Albtelecom" has just been passed by the Parliament.

Although foreign direct investment has increased recently (three-fold compared to previous years) due to the successful privatisations mentioned above, it still remains limited due to structural impediments such as heavy administrative procedures, corruption in the judiciary and the public administration, poor infrastructure and a climate of occasional insecurity, despite considerable progress in consolidating law and order. Financial sector reform has progressed, but further efforts are needed to enhance the legal, regulatory and supervisory framework of the banking sector.

- Implementing the Growth and Poverty Reduction Strategy.
- Developing implementation and monitoring mechanisms for the MTEF.
- Continued efforts in strengthening tax collection and reducing tax evasion.
- Reducing corruption and fraud.
- Boosting the restructuring and privatisation of large-scale enterprises in the strategic sectors.

- Making the National Investment Promotion Agency operational and taking measures to protect foreign investment.
- Implementation of the power sector action plan.

Regional Co-operation

Albania has committed itself to playing a constructive role in the region, be it at the bilateral or multilateral level. The Albanian authorities signed many agreements with neighbouring countries in the period from January 1998 to February 2001. Most of these are co-operation agreements in the educational, cultural and economics spheres. Albania is currently working towards establishing a free Trade Area with FYROM and has increased significantly its co-operation with its EU neighbours in the field of Justice and Home Affairs. In the context of the difficult political situation in neighbouring FYROM, Kosovo and Southern Serbia, Albania has clearly condemned the actions perpetrated by the ethnic Albanian extremist groups, aligning itself with the positions of the international community. In the case of FYROM, it has been pursuing a constructive dialogue both with the authorities and with the ethnic Albanian political leaders. Albania has also improved its relations with FRY through the re-establishment of diplomatic relations. It is actively engaged in the Stability Pact as well as in other regional fora (SECI, SEECP).

- Continuing efforts in co-operation with and the assistance of the international community in combating organised crime and illegal trafficking from and through its territory, by further enhancing the policing of its borders (FRY/Montenegro - Kosovo and FYROM).
- Strengthening co-operation with regional neighbours in the fields of Justice and Home Affairs - as agreed to in the Zagreb Summit - as well as implementing relevant Stability Pact Projects.
- Continuing to use her influence with ethnic Albanian communities in neighbouring countries to promote peace and stability.

2. Operational conclusions

The Council welcomed the Report by the Commission on the work of the EU-Albania High Level Steering Group. It recognised the substantial progress made by Albania and therefore invited the Commission to build on this dynamic with a view to an early presentation of draft negotiation directives for the negotiation of a Stabilisation and Association Agreement with Albania, if possible before the end of the year.

In order to support the ongoing reform process and in view of preparations of the future SAA-negotiations, the Council has agreed that a joint Consultative Task Force with Albania shall be set up, as soon as possible.

B) Bosnia and Herzegovina

For the first time in 10 years, the State government and the government of the Federation of Bosnia and Herzegovina (FBiH) are formed by non-nationalist parties of the multi-ethnic "Alliance for Change", which has expressed its commitment to multi-ethnicity and European integration. In the Republika Srpska (RS), Prime Minister Mladen Ivanic is following a pragmatic course in his support for the "Alliance" at State level. In its relations with the EU, the goal of the new Council of Ministers is to complete the Road Map. Top priorities include i.a. the Election Law, the Civil Service Law, implementation of Property Laws and conditions for sustainable returns.

Still, tensions remain. Bosnia and Herzegovina's (BiH) special problems are exemplified by two current issues: (i) a stand-off with HDZ-inspired "Croat self-rule", mostly in Herzegovina and characterised by systematic intimidation and occasional violence; (ii) the eruption of violence

in Trebinje and Banja Luka (RS) as work began on reconstructing Muslim mosques. Acceptance of integration is far from universal.

Despite over US\$ 5 billion in aid, BiH remains one of the poorest countries in Europe (GDP \$972 per capita); its GDP is just over half the pre-war level. Growth rates have declined due to a decline in donors' assistance (2000 +10-12%, 2001 est. +4-5%). Given limited domestic resources, BiH must move from donor-driven to investment-driven growth, but the conditions for attracting foreign direct investment remain poor.

1. Issues needing special attention

Democratic Principles

Progress in fulfilling outstanding Road Map criteria and in advancing the peace process is hampered by nationalist obstruction delaying BiH parliamentary legislative steps. The never-ending battle between those favouring strengthening the State vis-à-vis those safeguarding entity powers is keenly felt at present. The constitutional challenge of the HDZ/CNC-led "Croat self-rule" and setbacks to the peace and reconciliation process in the RS have greatly compounded the State-building process. The Council of Ministers rests on a frail majority and has little time to produce results before the 2002 elections. Adoption of civil service and election laws are important Road Map criteria. The wartime divide between Bosniacs, Serbs and Croats remains deep. Lack of political will and optimism for the future, and widespread corruption, are main reasons for the slow pace of reintegration and reconciliation.

Political influence over the media is common. Recently, the media picture has deteriorated in Croat-controlled areas due to the so-called "Croat self-rule". Strengthening independent media and building the Public Broadcasting System (PBS) are very important. In early May, PBS radio began broadcasting.

- Compliance with the General Framework Agreement for Peace (GFAP) - ICTY, elimination of parallel power structures (especially in the FBiH) etc.

- Adoption of an election law and organisation by the BiH authorities of free and fair elections (next due in 2002).

- Strengthening functional and democratically accountable common institutions, especially at BiH State level, and adoption of the Civil Service Law.

- Strengthening Civil Society.

- Strengthening an independent media landscape.

Human Rights and Rule of Law

In general, there is a slow but steady trend towards an improved human rights situation.

However, there are considerable human rights problems in the country. Attacks on minority returnees, journalists and politicians occur. Discrimination along ethnic lines is common. The educational sector is largely ethnically segregated.

Ensuring that the BiH Constitutional Court's decision on "constituent peoples" is thoroughly implemented is probably the single most important way to strengthen human rights in BiH. The entity parliamentary Constitutional Commissions are now drafting amendments for the

Harmonisation of the entity constitutions with the BiH one. Strengthening the rule of law by establishing a truly independent judiciary continues through the judicial review process.

Continued reform of BiH police forces is necessary.

- Strengthening of the legal system inter alia through sufficient well-trained judges.
- Strengthening the rule of law through judicial reform, police reform and State Border Service (SBS) build-up to fight crime and corruption.
- Strengthening the fight against organised crime, corruption and trafficking in human beings.

Respect for and Protection of Minorities

Until the entity constitutions are amended, making Bosniacs, Serbs, Croats and others constituent peoples throughout BiH, their rights are not fully protected. The Council of Ministers has drafted a law on the rights of ethnic minorities, which will be discussed with the entities and with ethnic minorities prior to submission to parliament. As currently drafted, the law defines 17 ethnic groups as minorities. Each minority would have the right to education in their own language in areas where they constitute a majority, and in areas where they constitute more than three percent they would be entitled to participate in the local authorities.

Regarding return of refugees and displaced persons, minority returns in BiH have doubled in the first three months of 2001 compared with 2000. However, refugee return-related violence occurs. Property law implementation is slow and often obstructed by local authorities. Repossession efficiency rates vary greatly and are on average 13% in the RS and 32% in the Federation. This process must be accelerated.

- Implementing the BiH Constitutional Court's ruling on constituent peoples.
- Ensuring the rights of minorities.
- Strengthening the conditions enabling sustainable refugee returns in line with the Dayton/Paris agreement.

Market Economy Reform

The BiH economy is in dire straits. Living standards are bleak for most citizens. Unemployment averages 40%. The potential risk for increased strikes and growing social unrest is high. The Council of Ministers has few sources of own revenue, relying to some 75% on entity contributions.

The fiscal stance of the entities, particularly of the RS, is a cause for concern. Economic reforms must be pushed vigorously by the Council of Ministers. Creating a single economic area in BiH and removing all inter-entity trade barriers are crucial for economic progress. BiH must move from donor-driven to growth increasingly relying on domestic forces. Attracting foreign direct investment must be a top priority. The poor investment climate must be improved by easing cumbersome administrative regulations. Private sector development must be encouraged and privatisation accelerated. Increasing compliance with and enforcement of customs and taxation policies are crucial to combat widespread smuggling, fraud and tax evasion. The single BiH standards institute imposed by the High Representative must be approved by the BiH Parliament and adequately funded. Competition and consumer protection legislation must be enacted.

- Continuing ongoing economic reforms, especially the creation of a Single Market, and furthering privatisation.
- Rationalising and reducing the entities' military expenditures.
- Increasing tax collection and independent Council of Ministers revenues.
- Attracting Foreign Direct Investment by appropriate legislation, including Property Laws implementation, Competition and Consumer Protection Law and for a single BiH National Institute of Standards.

Regional Co-operation

Strengthening bilateral relations with Croatia and FRY are crucial prerequisites for the peace process to advance. The recent establishment of Inter-State Councils for Co-operation with Croatia and FRY are good signs that relations are improving. As GFAP signatories, Croatia and FRY have significant responsibilities and influence on BiH developments.

BiH has increasingly become a transit country for illegal migration to the EU. Regional co-operation in the area of justice and home affairs is of the utmost importance. The Sarajevo Joint Declaration of 28 March, adopted by BiH and its neighbours as a follow-up to the Zagreb Summit on regional co-operation in the area of asylum and immigration, must be implemented in earnest.

Securing funding for the further build-up of the State Border Service (SBS) is crucial for BiH to take full control of its borders. On 4 May, a UNMIBH-sponsored agreement on regional co-operation to fight organised crime and trafficking was concluded between the interior ministers of Croatia, FRY and the BiH entities.

- Developing good neighbourly relations, in particular with FRY and Croatia.
- Establishing effective border control, including adoption of the Law on the State Border to fight illegal migration, in line with the Sarajevo Declaration of 28 March.

Compliance with International Obligations and Peace Agreements

Five and a half years after the signing of the GFAP, a massive international involvement in BiH is still needed for the peace implementation process to advance. Despite efforts by the local governments, BiH is still far from being a viable State with sustainable structures that can take sole ownership for the implementation of the Dayton Agreement. Thanks to efforts by the High Representative W. Petritsch and other internationals, which make up for the lack of political will in BiH, the peace process inches forward. The so-called "Croat self-rule" is an illegal parallel structure that must be eliminated. ICTY co-operation is dismal, particularly as regards the RS. No arrests of persons indicted for war crimes (PIFWC)s have been initiated by RS authorities. The draft RS law on co-operation with ICTY must be accompanied by swift action.

- Further efforts to fully comply with the Dayton/Paris agreement.
- Continued efforts towards full co-operation with the ICTY, particular as regards RS.

2. Operational conclusions

The Council expressed its appreciation for the efforts by the new Council of Ministers in BiH to move forward on the path towards European integration. It recalled that the Zagreb Summit

called on BiH to fulfil the EU Road Map by the middle of 2001, so that the Commission could undertake a feasibility study as the next step in the Stabilisation and Association process. The Council looked forward to receiving a report from the Commission on the state of completion of the Road Map.

C) Croatia

Croatia is overall a stable democracy and evident progress has been made in the reform process since the change of government in January 2000. Constitutional reform and a clearer re-balancing of institutional powers were important achievements. The authorities are still confronted by structural problems and the consequences of the relative isolation of the economic system in the past. Further efforts are needed to meet the challenges of the transition process and to fully implement the ambitious reform agenda.

Croatia is one of the economically most developed countries of the region (GDP/capita estimated at \$ 4,230 in 2000). After a short recession, GDP started to grow again in the last quarter of 1999, albeit at modest levels and owing to favourable external factors. The overall macroeconomic situation is encouraging, with positive growth in 2000 (3.7% with respect to the previous year), relatively low inflation (4.5% at end year), stable exchange rate and a comfortable current account position expected for 2001.

1. Issues needing special attention

Democratic Principles

The government has been making efforts to enhance political freedoms and transform Croatia into a liberal and more stable democracy. The process of effective decentralisation and strengthening of local government has started and some devolution of powers to the local level formulated in a new law will enter into force on 1 July. Several other parts of the necessary reforms are awaiting decision. A new election law has been passed which provides for democratic elections. However, improvements are deemed necessary regarding representation and participation of minorities. Parliament has passed a new law on the HRT, while the new law on Telecommunications, which will be an important part of the privatisation process, is presently under Parliamentary procedure. The transformation of HRT into a public service broadcaster has however not yet happened and no final decision has been taken on privatising the remaining State-owned press (Vjesnik and Slobodna Dalmacija). Privatisation of the 3rd channel, as recommended by the Council of Europe and the OSCE, should take place in full transparency.

- Pursuing an effective decentralisation and strengthening of local government.
- Improving the procedures for implementation of the provisions in the new election law for minority representation.
- Continuing the reform of the broadcast media with the final adoption of the Law on Telecommunications, including the privatisation of the 3rd TV channel in full transparency.

Human Rights and Rule of Law

The Government of Croatia has initiated a substantial reform of the legal framework governing the democratic institutions. These efforts need to be further pursued. The necessary reforms should include both extensive legislative changes and an administrative overhaul of the judicial system. As for corruption, a decision has been taken to establish an independent anti-corruption agency (USKOK), but actual implementation is pending.

- Pursuing substantial reform of the judiciary to underpin the democratic process.
- Implementing the government's commitment to fight corruption through concrete action.

Respect for and Protection of Minorities

Rights and freedoms are in general respected, but there is still room for improvement as regards rights of persons belonging to national minorities. The already prolonged deadline (May 2001) for a new "Constitutional Law on the Protection of Human Rights and Fundamental Freedoms and on the Protection of the Rights of Ethnic and National Communities and Minorities" has expired, without any evidence that a proposal is about to be presented to Parliament. The government recently announced a new and more decisive policy on refugee returns (the 'Knin conclusions'). In addition to these efforts, steps still need to be taken to ensure continuous and sustainable refugee return in the war-affected areas. The unreformed legal regime of repossession of property, including the issue of lost occupancy and tenancy rights, remains a significant obstacle. Further action is required to ensure that evictions take place in cases of multiple and illegal occupancy. The OSCE has outlined the relevant decisions on legislative and administrative changes that need to be taken to achieve a sustainable refugee return.

- Adoption of the new "Constitutional Law on the Protection of Human Rights and Fundamental Freedoms and on the Protection of the Rights of Ethnic and National Communities and Minorities"

- Fully implementing the refugee return process. This includes continued constructive dialogue and co-operation with the Bosnia and Herzegovina and FRY authorities. Continued efforts are needed on promoting return, creating sustainable conditions for it, securing repossessions and solving the problem of ineffective Housing Commissions, and providing alternative accommodation.

Market Economy Reform

Croatia has a solid industrial base, a qualified and educated workforce and areas with great potential for development like tourism. The consolidation of the banking sector continues and the confidence of banks and depositors seems to be returning. A new Central Bank law has been adopted recently which corresponds to international standards and gives the Central Bank wider authority and independence. A mixture of slow economic growth over the past years, dragging restructuring and modernisation of the economy and wage increases above productivity gains have resulted in high and rising unemployment (reaching a rate of 22.9% in March 2001). More efforts are needed to eliminate administrative obstacles and simplify bureaucratic procedures, which still hamper private sector development. Reform in this area is a necessary prerequisite for attracting foreign direct investment on a larger scale. A fundamental restructuring is necessary to obtain a market economy with a slimmed-down, efficient, decentralised public sector. The necessary reforms required with a view to the implementation of the SAA within the economic policy sphere will require a particular effort. Positive macroeconomic developments will depend greatly on the pursuance of a judicious combination of fiscal adjustment, wage discipline and structural reforms in the context of continued exchange rate stability, as well as on strict obedience to the reform programme agreed with the IMF and the World Bank. On 19 March 2001, a Stand-by Arrangement (SBA) with the IMF was approved, which provides an important framework of economic policy-making and monitoring in this respect.

- Pursuing a stable and sustainable fiscal policy including a reduction of the public wage bill.
- Streamlining the large public sector including privatisation.

- Improving the legal framework and creating the conditions for private sector development, in particular the tourist sector.
- Strengthening the pension and health care systems.
- Enforcing active employment measures (training, education).

Regional Co-operation

Croatia has a major role to play in the durable stabilisation of the region. Relations with Bosnia and Herzegovina have come to the forefront, and the government of Croatia has urged the Bosnian Croats to look for solutions within the constitutional and institutional framework of Bosnia and Herzegovina. Contacts between government officials and their Yugoslav counterparts are generally positive, but the dialogue with the FRY needs to be further enhanced. Regional co-operation, notably on justice and home affairs, will be an important issue under the Stabilisation and Association Agreement. Recently a co-operation agreement on illegal migration and organised crime has been signed with Bosnia and Herzegovina and the FRY.

- Pursuing efforts to develop fully transparent relations with Bosnia and Herzegovina and to improve relations with FRY to solve outstanding issues, notably Prevlaka.
- Initiating negotiations on a convention on regional co-operation with FYROM, as required under the SA Agreements, as soon as possible.
- Ensuring that expulsions of unwanted aliens take place only to the countries from which they entered Croatia.
- Any challenges or provocation to the common BiH institutions should continue to be condemned.

Compliance with International Obligations and Peace Agreements

Croatia has taken positive steps to co-operate with ICTY, but there is a continued need for full compliance with ICTY obligations. The EU recognises that overall relations between Croatia and Bosnia and Herzegovina have been strengthened. The government of Croatia has also made an earnest effort to reduce its transfers to the Croats in Bosnia and Herzegovina, and to make those transfers more transparent. After disturbing international reports, the government of Croatia is now asking for an audit of its own of last year's transfers, while withholding the transfers included in the State budget for this year.

- Continued efforts need to be undertaken to fully comply with the Dayton/Paris and Erdut agreements.
- Continued efforts towards full co-operation with ICTY, including the transfer to The Hague of Croats indicted for crimes committed on Croatian soil.
- Increasing transparency in relations with neighbouring Bosnia and Herzegovina, in particular in the field of financial transactions to the Bosnian Croats.

2. Operational conclusions

The Council welcomed the initialling of the Stabilisation and Association Agreement with Croatia on 14 May as a historic step in Croatia's integration into European structures. The future signing of the Agreement, and the conclusion of the Interim agreement, will for the first

time establish mutual contractual relations between the Union and Croatia. Ahead of the entry into force of the Interim and the Stabilisation and Association Agreements, including their institutional arrangements, the Council agreed that the Joint Consultative Task Force should be maintained and that a Political Dialogue be formalised by means of a Joint Declaration between the EU and Croatia.

D) Federal Republic of Yugoslavia

The Federal Republic of Yugoslavia is today a full participant in, and beneficiary of, the Stabilisation and Association Process. Less than eight months after the "democratic revolution", the Federal and Serbian governments have made progress in many fields although the inherited challenges are still immense. Further to consolidation of political structures, focus has been on reforms aiming at creating the basic conditions for the market economy to operate. The Donors' Conference for the FRY scheduled for 29 June has turned into a clear goal for the authorities. A further priority is resolving the future constitutional relations between Serbia and Montenegro, through an open dialogue and a spirit of compromise, aiming at an agreed redefinition of their relations in a renewed federal framework according to democratic principles. This would also speed up the ongoing reform process. Belgrade has played a crucial and constructive role in resolving the crisis in Southern Serbia. This issue, and the developments in Kosovo, as well as the effects of the tense situation in FYROM, have nevertheless diverted attention from other aspects of the internal reform process.

1. Issues Needing Special attention at Federal/Serbian and Montenegrin Level and in Kosovo

i) At Federal/Serbian Level

Democratic Principles, Human Rights and Rule of Law

Respect for democratic principles, human rights and the rule of law has improved at the policy level. A number of new laws have been adopted, e.g. the amnesty law adopted at the beginning of March. A "Truth Commission" has been set up to promote an open and transparent process in the investigation of crimes. A large number of persons connected to the former regime and under suspicion of abuse of power, economic crime and murder have been arrested or are under investigation. An anti-corruption agency has been created and an anti-corruption law is being prepared. A department for combating organised crime has been set up and the government has proposed the formation of a parliamentary committee to control the State Security Service. A resolution presenting a Code of Conduct for State officials has been passed to Parliament suggesting also the establishment of a control body for the State administration. A new republican penal code has been proposed to Parliament.

But much remains to be implemented, particularly in the field of judicial reform, media independence and rights of persons belonging to national minorities. Around 260 prisoners of ethnic Albanian origin still remain in prisons, some of whom are presumed to be political prisoners. Furthermore, the issue of missing persons from the Kosovo conflict remains to be effectively addressed. Fighting organised crime and corruption is among the most difficult challenges ahead. The three highly political cases (Curuvija, Stambolic and Ibarska highway) remain unsolved. The new republican penal code, which has been proposed to Parliament, will require harmonisation between the federal and republican levels. The fact that the death penalty is maintained in the new penal code is a matter of deep concern. Improvements and structural reforms at policy level need to be followed up with clear timetables for implementation - particularly in the field of judicial reform.

- Resolving the issue of remaining Kosovo-Albanian prisoners, as well as the issue of missing persons.

- Removing remaining restrictive legislation from the statute books.

- Urgent abolition of the death penalty from the republican penal code.
- Developing an independent media sector and promoting a healthy media climate.

Respect for and Protection of Minorities

The situation of national minorities has improved since September last year. A new law on national minorities is being drafted, as is a law on local self-government. But the situation on the ground for minorities (such as Roma and/or ethnic Albanians) remains difficult in many parts of the country. Efforts should continue with the ambition to place all citizens on an equal footing legally, economically and socially. Also, the commitment by the Serbian government to confidence- building measures in Southern Serbia is highly welcome, as well as their swift implementation.

- Strengthening further the rights of people belonging to national minorities and vigorously tackling discrimination and prejudice against minorities.
- Adopting the Law on local self-government.

Market Economy Reform

The entry of the FRY into the International Financial Institutions is important, as is the temporary and exceptional access to IDA resources granted by the World Bank. A stand-by arrangement with the IMF is being finalised. Progress has been made in restoring macroeconomic stability and starting the process of transformation from a command economy to a modern market economy. Positive steps have been the adoption of new employment laws, a law on extraordinary taxation of revenues and on properties acquired improperly during the Milosevic era, as well as a new law on privatisation. Some progress has also been made in the fiscal sphere, most notably with a first attempt at budget consolidation and tax simplification. However, FRY transition has just started and the reform agenda remains huge. Further progress will be necessary in particular in:

- the rationalisation of public expenditures, including the reduction of military expenditure;
- the creation of a legislative, institutional and policy framework conducive to the development of the private sector;
- the privatisation of socially owned companies and State companies;
- the adoption of a law on foreign investment, guaranteeing the rights of all investors;
- the enhancement of public administration (legal framework, accountability, reduction of discretion in administrative decision-making, etc);
- fighting corruption.

Regional Co-operation

Diplomatic relations have been established with all neighbouring countries and regional co-operation has significantly improved. Belgrade is developing contacts with the BiH-level institutions in Sarajevo, while continuing to develop its special links with Republika Srpska. More recently, Ministers of the Interior from the FRY, Croatia and BiH signed an agreement on co-operation in the area of organised crime and illegal migration. The resolution of outstanding refugee issues remains to be effectively addressed. In relations with Croatia the outstanding regional issue of Prevlaka awaits settlement.

- Undertaking at regional level co-ordinated efforts to resolve refugee issues relating to property rights, and /or economic and social reintegration for those wishing to return by their free will.
- Giving full support to the Dayton process in relations with BiH and giving privilege to the common BiH state institutions. Any illegal challenges or provocation to the common BiH institutions must be clearly condemned.
- Pursuing regional co-operation and reconciliation e.g. within the framework of the Stability Pact, the SEECP and other relevant fora. This includes the resolution of outstanding regional issues, such as Prevlaka.

Compliance with International Obligations and Peace Agreements

A new atmosphere of dialogue characterises the FRY's relations with regional and international interlocutors. FRY has taken a more co-operative stance towards the ICTY. Positive measures have already been taken, such as the arrest and transfer of one indictee as well as the arrest of former President Milosevic. Much remains to be done. The new government has to meet all its international obligations and should continue on the path towards full co-operation with ICTY.

It is also crucial that Belgrade's positive dialogue with UNMIK continues, in order to ensure the participation of Kosovo Serbs in Kosovo society, including in Kosovo-wide elections.

- Undertaking further efforts to fully comply with the Dayton/Paris and Erdut agreements, including efforts towards full co-operation with ICTY. This entails full compliance with UN Security Council Resolution 827, supplemented by the rapid adoption of the appropriate legal framework. Practical steps need to be taken to preserve and provide ICTY with access to evidence and further co-operation on the hand-over of indictees.
- Ensuring a genuine commitment to UNSC resolution 1244 and a continuing active and structured relationship with UNMIK.

ii) At Montenegrin Level

Democratic principles, Human Rights and Rule of Law

In general there is continued respect for democratic principles, human rights and rule of law. The commitment to reform in Montenegro is strong, this has so far resulted in concrete reform measures in the economic sphere. However, much of the political energy in Montenegro has been consumed by the unsettled relations within the Yugoslav federation and the reform process in many other areas remains to be converted into concrete measures. Several draft laws reforming the judiciary and the public sector await adoption, such as the laws on public prosecutors, on courts and in the municipal area. Transparency within the public sector remains to be improved, such as measures aimed good governance, and the police is disproportionately large and unreformed. Furthermore, some questions remain concerning media independence and standards.

- Enacting draft laws concerning the judiciary, the municipal level, aiming at reform, transparency and good governance.
- Initiating thorough reform of the police.
- Assuring media independence in accordance with international standards.

Respect for and Protection of Minorities

The constitutional provisions for minorities are good and the practice is generally functioning satisfactorily.

- Vigorously tackling non-official discrimination and prejudice against minorities.

Market Economy Reforms

Montenegro's macroeconomic situation had steadily deteriorated during a decade of gradual dissolution of the Socialist Federal Republic of Yugoslavia, disruption of trade patterns, wars in the region and economic decline in the larger Serbian market, and the outbreak of the Kosovo crisis.

The Montenegrin authorities moved towards a more independent policy stance towards the end of 2000, inter alia unilaterally adopting the D-mark/€ as sole legal tender. Macroeconomic stability has been broadly maintained, but mostly due to large inflows of foreign grants, covering the fiscal deficit of the Republican budget. On the structural side, various reform measures have been undertaken in the area of public finance (improvement in accounting standards, adoption of an organic budget law and measures to enhance revenue collection), as well as in the monetary area (central bank law). These steps were largely enforced through conditionality attached to the exceptional Community financial assistance provided in 2000.

Further progress is necessary, particularly in:

- further restructuring of public finances, most notably through the introduction of a Treasury system to improve expenditure control;
- promoting the privatisation process in a transparent manner;
- enhancing further reforms of the banking sector;
- supporting small and medium-sized enterprises;
- combating corruption and organised crime, smuggling and trafficking;

iii) Kosovo

The international community is committed to the full implementation of UNSCR 1244. UNMIK and KFOR are working towards establishing a peaceful, multi-ethnic, multi-cultural and democratic Kosovo. In this context, the adoption of the regulation concerning the constitutional framework for provisional self-government in Kosovo is an important step in the implementation of UNSCR 1244. It will provide the basis for Kosovo-wide elections to be held on 17 November. The further development of co-operative relations between Belgrade and UNMIK will also be a priority for building confidence among the Kosovo-Serb community, which should assist in the organisation of Kosovo-wide elections.

The establishment of a secure environment for all the people of Kosovo remains a priority. More improvements must be made in respecting human rights as well as in strengthening the rule of law. In particular, the proper functioning of Kosovo's judicial system has to be ensured.

Much has been achieved in establishing and developing a market economy, under the guidance of EU pillar of UNMIK. However, private investment is still lacking due to insecurity and ownership problems and future status. In the economic domain, private sector development including privatisation is a key priority. To this extent, rapid progress is needed in creating or completing the essential legal and institutional basis.

2. Operational conclusions

The Council welcomed the important progress achieved by the FRY in consolidating democracy and in promoting the necessary economic and legal reforms, including its efforts to continue on the path towards full co-operation with ICTY. Recalling the perspective as outlined at the Zagreb Summit, the Council agreed to hold the first meeting of the EU-FRY Consultative Task

Force, if possible by the end of July, as a first step towards a Stabilisation and Association Agreement. The Council looked forward to a successful Donors' Conference on 29 June.

E) Former Yugoslav Republic of Macedonia

The political situation is tense following the actions of the ethnic Albanian extremists of the "National Liberation Army" which started in March 2001. As a consequence, inter-ethnic relations have deteriorated considerably in the last few months, and it has become obvious that this is the single most important issue facing the country. Thus, a Government of National Unity has been established to overcome the crisis, to engage in an effective inter-ethnic dialogue and to address overall reforms in line with the Stabilisation and Association Agreement (SAA), including legitimate concerns over the rights and status of minorities. As a result of the visit of High Representative Solana to Skopje on 28-29 May, the four party leaders committed themselves to achieving substantial progress on the President Trajkovski reform agenda by June 15.

Macroeconomic developments were encouraging in 2000, as real GDP grew by 5.1%. FYROM made progress with economic reforms and institution-building. The nation is classified as a lower/middle income country and GDP/capita stood at USD 1885 in 2000. In late 2000 macroeconomic policies started to slip and additional military expenditure due to the crisis will burden government finances while structural reforms, including privatisation, appear to be stalling.

1. Issues needing special attention

Democratic Principles

Democratic principles are generally respected, and the democratic process functions normally overall. However, inter-ethnic tensions have increased dramatically in the current crisis. The enhanced inter-ethnic dialogue has been established to make speedy progress in the reform process, e.g. to strengthen local self-government and the integration of under-represented ethnic groups into the administration. There are shortcomings in the Law on Local Elections and the role of the State Election Commission is undefined. The new broader coalition government has, however, a reform of the election law including the election commissions high on its agenda. Lack of participation of MPs in Parliamentary meetings is causing deliberate delays in adoption of important legislation. The media landscape gives room for freedom of expression, but the State-funded media are in the control of the parties in power on an alternate basis and there has been no attempt to transform the State broadcasting company into a "public service".

- Continuing inter-ethnic dialogue at institutional and civic level on necessary reforms (i.a. social and non-governmental organisations, local government, religious leaders and business).

- Developing an appropriate election process including amendment of the Law on Elections to clarify the role of the State Election Commission and the financing of elections. Development of civic education on the conduct of elections;

- Clarifying the status of the Broadcasting Council and its independence from government and strengthening its legal position. A plan should be developed to transform the State broadcaster into a "public service broadcaster".

- Adoption of 3rd Channel in Albanian Languages;

- Adoption of the new Media Law in conformity with international standards.

Human Rights and Rule of Law

Human rights are generally being respected, but there are shortcomings in several areas: the independence of the judicial system needs further consolidation. Many international conventions have been ratified, but need now to be implemented. Impartiality on the part of the police and tax authorities should be ensured. Prison conditions need to be improved. The role and responsibilities of the law enforcement authorities need to be clarified.

- Completing the current process of reform of the judiciary.
- Implementation of the Public Administration Reform.
- Strengthening institutional capacity to deal with corruption, cigarette smuggling, money laundering and international organised crime.

- Structural reform and training of the law enforcement authorities.

- Facilitating and enabling the return of refugees and internally displaced persons, ensuring right conditions, including reconstruction of houses in areas affected by the conflict.

Respect for and Protection of Minorities

Inter-ethnic relations continue to be the single most important issue. The adoption of a new law on education in July 2000 was a major improvement in regard to higher education in Albania, but secondary education in Albanian still remains a concern. The Roma continue to be the most disadvantaged group from a socio-economic point of view.

- Providing a clear timetable to address, in the course of this year, legitimate concerns over the status of minorities and their ability to play a full role in the political, economic and administrative life of the country by recognising the multi-ethnic nature of the country.

- Proceeding with the political dialogue on ethnic issues (inter alia local self-government reform, integration of minorities into the public administration including in particular the police as well as the army, use of minority languages in the courts and public authorities, notably the Parliament.

- Undertaking a census of the population in consultation with the international community, in line with international standards.

- Ensuring the opening in October of the South East Europe University in Tetovo.

Market Economy Reform

In 2000, FYROM signed agreements with the IMF and the World Bank on a new economic programme that could be supported by credits from the International Financial Institutions (IFI). However, the IMF is currently revising the programme in the light of severe economic policy slippages and the recent crisis in the country, which will put a strain on government finances. Progress with new legislation, notably banking and insurance legislation, as well as privatisation, was encouraging in 2000, but the reform pace is currently slowing down, posing a risk to the medium and longer-term growth prospects. The privatisation process, notably regarding large loss-making enterprises, should be strengthened and made more transparent. The closer economic links with the European Union in the context of the SAA and the unilateral trade measures in favour of FYROM provide an opportunity to strengthen economic transition. However, only a minor range of FYROM products is currently competitive in the EU market.

- Efforts to maintain economic equilibrium and a satisfactory track record on economic policy measures agreed with IFIs.

- Restructuring of public finances, completion of the privatisation process, and compliance with IFIs' conditionality, most notably with regard to selling or closing State-owned loss-making enterprises.

- Promotion of competitiveness through market-based enterprise restructuring, development of small and medium sized enterprises.

- Taking measures to stimulate domestic and inward investments and further reforms of banking and insurance sectors.

Regional Co-operation

FYROM is very active in strengthening regional co-operation. It has taken important steps by entering into bilateral free trade agreements (FTAs) with its neighbours, and furthering a network of FTAs including through the Stability Pact. It has also been actively encouraging improved regional co-operation within the framework of the SEECP. The Government is aware of the problem of organised crime, smuggling of arms, cigarettes and drugs, and trafficking in women. Regional co-operation, notably on justice and home affairs, will be an important issue under the Stabilisation and Association Agreement as well.

- Starting negotiations with Croatia, as soon as possible, on a convention on regional co-operation as required under the Stabilisation and Association Agreement.

- Continuing to enter into bilateral free trade agreements with neighbouring countries to establish Free Trade Areas, thus contributing to the creation of a network of Free Trade Agreements.

- Giving priority to addressing problems of illegal migration and trafficking in human beings, preferably in co-operation with neighbouring countries, for instance through signing up to the agreement on illegal migration and organised crime recently approved by Croatia, Bosnia and Herzegovina and the FRY.

2. Operational conclusions

The Council welcomed the signing of the Stabilisation and Association Agreement with FYROM on 9 April and the entry into force of the Interim Agreement on 1 June. It called upon all political leaders to rapidly achieve concrete and substantial results on inter-ethnic dialogue and to make further progress on overall reforms, thereby accelerating FYROM's progress along the road to Europe under the Stabilisation and Association process.

VI. Conclusions

Conditionality in all its guises is at the heart of the Stabilisation and Association process, as confirmed by the GAC conclusions of 9 April 2001. The establishment of a substantive review mechanism, based on a report prepared by the Commission, has provided the means to assess each country's performance and respect for the conditions of the Stabilisation and Association process. It allows the EU to assist the countries to progress at their own pace, in accordance with the operational conclusions as set out for each country above.

The above country assessments reflect priorities identified and recommendations on action to be taken for Albania, Bosnia and Herzegovina, Croatia, FYROM and FRY. The EU will expect each country to pay special attention to and to devote the necessary resources to the priority areas for action identified in these reviews.

The present report on the Stabilisation and Association Process represents a first political review. A full review, including an assessment of the efficiency of the Stabilisation and Association process instruments, will be undertaken before the end of this year, and then on an annual basis. Notwithstanding the annual review, the Council will, on a continuous basis, follow overall developments in the countries concerned.

General Affairs Council, Luxembourg, 11 June 2001

ANNEX COUNCIL REPORT - Review of the Stabilisation and Association Process

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I. Introduction

The Stabilisation and Association Process represents the European Union's commitment to contribute to peace, democracy and prosperity in South-Eastern Europe. In line with the General Affairs Council's decision of 9 April 2001(1) to undertake annual reviews of the countries of the Stabilisation and Association process, and the decision to conduct an early, political review already in June 2001, the Council has prepared an assessment of each country in the context of the strategic objectives of the Stabilisation and Association process. The first part of this report explains the overall rationale behind the Stabilisation and Association process, its objectives and how it can allow the EU to help each country achieve sustainable reforms and to move closer to the overall goal of EU membership. This part is followed by a summary of country assessments, which contains recommendations for further action to be taken by the countries concerned, and operational conclusions relating to: Albania, Bosnia and Herzegovina, Croatia, the Former Yugoslav Republic of Macedonia and the Federal Republic of Yugoslavia.

II. From Regional Approach to the Stabilisation and Association process

After a period of violent conflict in the region the EU Regional Approach of 1997(2) sought to underpin the implementation of the Dayton/Paris and Erdut agreements and bring basic



stability and prosperity to the region. In June 1999 the EU(3) set out a more ambitious vision for the region's development. This was based on:

- a recognition that the main motivator for reform in these countries is a credible prospect of potential membership once the relevant conditions have been met(4), as offered at the Feira European Council. It clearly goes beyond the former offer of "contractual relations" (Trade and Co-operation Agreements) in the Regional Approach;
- the need for the countries concerned to establish normal mutual relations, which would allow greater economic and political stability in the region to develop;
- the need for a more flexible approach enabling each country to move ahead at its own pace.

This flexibility is balanced by a common set of political and economic conditions so as to maintain the integrity of the EU's overall policy towards the region(5).

In July 1999 the Stability Pact, which also contributes to the core aims of the Stabilisation and Association process, was launched.

III. The Stabilisation and Association process (SAP)

The Stabilisation and Association process is a long-term commitment to the region in terms of both political effort and financial and human resources. The process represents an overall framework in which preferential trade concessions, an assistance programme and a new contractual relationship should assist each country to progress, at its own pace, and on the basis of the implementation of necessary reforms, on the way towards the prospect of EU accession.

The 24 November Zagreb Summit set the seal on the Stabilisation and Association process by gaining the region's agreement to its objectives and conditions. The Summit stated in particular that "democracy and regional reconciliation and co-operation on the one hand, and the rapprochement of each of these countries with the EU on the other, form a whole". The countries of the region thereby undertook to abide by the EU's conditionality and use the Stabilisation and Association process, and in particular the Stabilisation and Association Agreements when signed, as the means to begin to prepare themselves for the demands of becoming candidates for EU membership some time in the future. Thus conditionality, as a policy addressing the region as a whole, is the cement of the Stabilisation and Association process.

a) Trade

The EU is by far the most important trading partner for the region. The promotion of trade flows is a core action for the EU within the Stabilisation and Association process. The Lisbon European Council of March 2000 stated that Stabilisation and Association Agreements should be preceded by asymmetrical trade liberalisation. Since December 2000(6), the EU has accordingly applied a highly preferential trade regime to all the countries covered by the Stabilisation and Association process. The opening of EU markets to products from the Stabilisation and Association process countries is intended to promote foreign investment, develop export capacities and contribute to the overall political and economic stability of the region. The granting of autonomous, preferential trade measures remains, however, subject to compliance with relevant Stabilisation and Association process conditions, including readiness to engage in effective economic reforms and in regional co-operation.

b) Assistance

EU assistance requires that certain political and economic conditions inherent in the Stabilisation and Association Process be met. CARDS(7) brings a more strategic approach to assistance to the countries concerned. It underpins the objectives and mechanisms of the Stabilisation and Association Process. As each country moves deeper into the process, assistance will focus increasingly on support for the reforms and institution building as required by the Stabilisation and Association Agreements. But this is not to ignore the political requirement of responding to crises, as necessary, and carrying out the massive reconstruction task the Community has been set. The challenge to Community policy is to respond effectively to volatility, while holding a steady course towards the strategic goal of integration into the EU.

c) Stabilisation and Association Agreements

Stabilisation and Association Agreements are a high-value political tool which, much as the Europe Agreements did for other countries, provide the formal mechanisms and agreed benchmarks whereby the EU can work with each country individually to bring it closer to EU standards. The Stabilisation and Association Agreements represent both the cornerstone of the Stabilisation and Association process and a key step towards its completion. The conclusion of Stabilisation and Association Agreements represents the signatories' commitment to complete, over a transitional period, a formal association with the EU. Such association is based on the gradual implementation of a free trade area and on reforms designed to achieve the adoption of EU standards, including enhanced co-operation, notably in the field of justice and home affairs, with the aim of a gradual rapprochement with the EU.

Differences between agreements for individual countries are likely to be reflected principally in the transition period towards full association with the EU and in the precise phasing and articulation of obligations. But the destination for all countries is expected to be the same: the full realisation of an association after a transitional period through implementation of the same core obligations.

- First phase: towards an Agreement

For the countries which are still working towards a Stabilisation and Association Agreement the "Consultative Task Force/High Level Steering Group" approach has proved an effective means of focusing authorities' minds on essential reforms and of engaging with them in a sustained way to secure implementation. The process is both pedagogical and political. It is based on clear objectives for reform, a work plan and a careful political judgement of how fast each interlocutor can realistically make progress.

- Second phase: implementing the Agreements

Effective implementation of the Stabilisation and Association Agreement is necessary for harmonisation with EU standards. The Stabilisation and Association Agreements do not, however, require signatories to endorse the whole of the EU acquis in one go. The focus is rather on respect for key democratic principles and the core elements of the EU acquis, which allow the EU single market to function properly. By extension through a free trade area with the EU and the associated disciplines (competition and state aid rules, intellectual property etc) and benefits (e.g. rights of establishment), this will allow the economies of the region to begin the process of integration into EU structures. For areas where the agreements do not impose specific obligations relating to the EU acquis there are provisions for detailed co-operation with the EU, again the purpose being to help each country to move closer to EU standards.

The Stabilisation and Association Agreements, then, are posited on respect for the conditionality of the Stabilisation and Association process agreed by the Council. But they also bring with them a dynamic means of operationalising that conditionality and give the EU the leverage necessary to get the countries to adopt genuine reforms with a view to achieving the

immediate objectives of the agreements. The mechanisms of the Agreements themselves will enable the EU to help prioritise reforms, shape them according to EU models, to address and solve problems, and to monitor implementation.

Signatories to the Stabilisation and Association Agreements should understand that effective implementation of the agreements is a prerequisite for any further assessment by the EU of the country's prospects of accession.

d) The Regional Dimension

The Stabilisation and Association process is not simply a bilateral process with each country. With the democratic changes in Belgrade it has become possible to tackle more common issues and objectives at a regional level. The Zagreb Summit placed considerable emphasis on the central need for regional co-operation as part of the EU's "contract" with the Stabilisation and Association process countries. Similarly, the Stabilisation and Association Agreements include a clear commitment to regional co-operation. The policy objectives are principally:

- to encourage the countries of the region to behave towards and work with each other in a manner comparable to that of EU Member States. An important means to this end will be the establishment of a network of close contractual relationships (conventions on regional co-operation) between the signatories of Stabilisation and Association Agreements;
- to create a network of compatible bilateral free trade agreements (as part of the conventions mentioned above) which would mean that there were no barriers to movement of goods between the countries of the regions nor between them and the EU and, in effect, neighbouring candidate countries;
- to achieve the gradual re-integration of the countries of the Stabilisation and Association process into the infrastructure networks (TENS) of wider Europe (transport, energy, border management);
- to ensure that the authorities in the countries of the region work together to respond effectively to the common threats which organised crime, drugs trafficking, illegal immigration and other forms of trafficking represent for the region's and the EU's security. In many cases, e.g. on visa policy, a common approach by all the countries will be needed to deal with the threat effectively. In this context, and as a follow-up to the commitments on justice and home affairs made at the Zagreb Summit, the countries of the Stabilisation and Association process have recently signed the Sarajevo Declaration on regional co-operation on asylum and migration.

Each country's contribution to achieving these objectives will help to determine the EU's assessment of that country's implementation of a Stabilisation and Association Agreement. The agreement on succession issues recently reached by the five Successor States of the former SFR of Yugoslavia represents a significant step towards reconciliation and normal neighbourly relations.

The Stability Pact complements the Stabilisation and Association process and will continue to be an important forum on which the Union can draw to further the strategic goal of the Stabilisation and Association process, in particular the dimension of regional co-operation. Constructive co-operation within the Stability Pact will therefore be recognised as a positive effort towards improving regional co-operation.

IV. Objective of the "Review Mechanism"

The range and depth of the new relationships embodied in the Stabilisation and Association process have not reduced the need for certain conditions to apply at all stages. The objectives of the EU's "Review Mechanism" in the Stabilisation and Association process are:

- to be able to regularly assess whether each country's level of compliance with Stabilisation and Association process criteria warrants the current level of engagement with the EU. In the event that this is not the case the Stabilisation and Association Agreements, the Autonomous Trade Measures Regulations and the CARDS Regulation provide for decisions on appropriate action;
- to provide a benchmark against which to judge how well a country is implementing the Stabilisation and Association Agreement;
- to agree on priorities for EU co-operation;
- to provide a tool for decisions on the further development of the relationship with the EU.

V. Country assessments

A) Albania

Domestic politics are dominated by preparations for the upcoming parliamentary elections scheduled for 24 June. Politics remain polarised, and personalities rather than policies still largely dominate the political debate. Despite progress achieved in ensuring public order and tackling criminality, state control in some parts of the country still remains weak. The stability of Albania is also influenced by forces outside the country, in particular by the situation in the ethnic Albanian inhabited territories across its borders and by organised crime. Albania has made great efforts to improve its relations with its neighbours, and has played a constructive role during the latest crises in the region, notably in FYROM and Kosovo.

The economy has been gaining in strength. In 2000, GDP grew by 7.8 % with respect to the previous year, while equal success was reached in the fiscal area, with a 25 % increase in tax revenues with respect to 1999 and a decrease in the fiscal deficit from 11.5% of GDP to 9.5% in 2000. Foreign financing of the deficit was consequently reduced from 6% to 4.5% of GDP.

1. Issues needing special attention

Democratic Principles

Albania's Constitution guarantees democratic freedoms such as political pluralism, freedom of expression and freedom of religion. Following adoption of the Constitution of Albania in November 1998, the authorities are in the process of undertaking major institutional reforms including the legal and judicial system. To this end, a number of new institutions have been and continue to be created, such as the appointment by the Parliament of Albania's first Ombudsman, the adoption of a new Electoral Code, the establishment of a complete Civil Service Commission, the establishment of the State Publication Centre and the School of Magistrates. Nonetheless, Albania needs to improve its performance considerably in the field of implementing democratic principles, as well as in that of institutional capacity, in order to achieve European and Community political standards.

Achieving such standards in practice means further strengthening the principle of separation of powers, by means of suppressing remaining interference between the legislative, executive and judicial organs.

- Completing the legislative framework in all fields and enhancing the capacity of the judiciary.

- Consistently implementing and better monitoring of the Anti-Corruption Plan.
- Holding free and fair elections in accordance with democratic principles, and carrying out outstanding improvements in the electoral process.
- Overcoming the country's confrontational political environment.

Human Rights and Rule of Law

Albania's Constitution guarantees respect for human rights. While the constitutional court ruled out the death penalty as unconstitutional in December 1999, in September 2000 Albania ratified the Convention on the Protection of Human Rights and Fundamental Freedoms and thereby took a further significant step towards European standards. However, implementation of existing rules need to be reinforced. The Council of Europe is currently preparing a report on the conformity of Albania's legislation and practices with the European Convention on Human Rights.

Civil society remains underdeveloped. It lacks sufficient financial resources as well as advocacy skills and in practice is not yet capable of playing its role in the country. Outside the capital, civil society is hardly present.

Freedom of expression and association is guaranteed in Albanian. However, in practice, the independence of radio and television needs reinforcing and the transformation of the State TV and Radio into an independent broadcasting institution needs to be completed. The opposition continues to breach the Law on Television and Radio, which requires it to participate in the National Council on Radio and Television.

The right of assembly and demonstration is in general respected in keeping with a recently enacted relevant law. However, there have been isolated cases where the treatment by the local authorities of detained persons has not abided by European norms and standards. The right to property is guaranteed in theory, but it needs further clarification and engagement with a view to creating a functioning and contemporary property and land market (cadastre).

Improvement in implementing the rule of law in Albania, along with sustained efforts to combat organised crime, should constitute the country's top priorities since they remain very serious problems, which hamper improvement in many other areas. The poor state of the judiciary, due to lack of qualified human resources, widespread corruption and party affiliation must be targeted for concentration of resources and attention. The poor working conditions, poor state of the Courts and Court Administration and poor performance and co-operation between the local prosecutor's office, the police and the judges needs to be urgently reversed.

- Completing the legal framework for the judiciary, and enhancing the training of judges.
 - Ensuring the proper application of human rights legislation by the judiciary and law enforcement agencies, including by means of improved training.
 - Improving the capacity of and co-operation between law enforcement bodies.
 - Enhancing the fight against organised crime, smuggling and trafficking in human beings.
- #### Respect for and Protection of Minorities

Albania's Constitution guarantees the rights of persons belonging to national minorities and in general these are respected. The most important minority in Albania is the Greek minority, however, there are also small communities of Slavo-Macedonians, Montenegrins, Vlachs and Roma. The Albanian government is committed to organising during the next few years a

census on the ethnic composition of the population as well as to presenting new minority legislation.

The Albanian government has committed itself to further improving the relevant legislation in order to adapt it fully to existing European standards. In September 2000, Albania ratified the Council of Europe Convention on the Protection of National Minorities, but it has not yet proceeded to implement the reporting obligations associated with its ratification. Albania guarantees the right to use minority languages in court proceedings, however, in practice, the costs of translation/interpretation must be paid by the interested party.

The Greek minority in Albania is organised through the association named Omonia and is represented at the political level through the Human Rights Union Party, currently in the ruling coalition. The minority enjoys normal access to the media. Last year's local elections were unfortunately marked by nationalistic overtones and a consequent rise in tension and irregularities in certain polling stations in the Himara municipality, where a sizeable ethnic Greek minority lives.

- Abolition of "minority zones", with the aim of ensuring the possibility for minorities to exercise effectively all their rights (i.a. property rights, the possibility to obtain education in mother tongue) throughout the country in accordance with Albania's international obligations.

- Drawing up a national strategy for their social and economic integration, namely for the Roma communities.

- Undertaking a census on the ethnic composition of the population in line with international standards.

Market Economy Reform

Continued progress has been made as regards macroeconomic stability as well as in implementing the pre-requisites listed in the Commission's Feasibility Report, despite the persistent structural weakness of the Albanian economy and the high percentage of the shadow economy. An important element expected to contribute to improved public expenditure management has been the adoption by the government at end of 2000 of the Medium-Term Expenditure Framework (MTEF) (2001-3). As for trade liberalisation, Albania became a member of the WTO in 2000 and is on track for fulfilling the commitments undertaken in this context. Indeed, it currently has no quantitative restrictions on imports or exports, and has reduced the maximum tariff rate from 18 to 15% (Jan. 2001). Due to the sizeable shadow economy, statistical data have to be carefully considered.

In the field of privatisation further progress was achieved with the full liquidation, lease or selling of all small and medium-sized enterprises in Albania by the end of 2000. Successful privatisation in June of the Albanian Mobile Communications company paved the way for the concession awarded to the second mobile telecommunications operator in February 2001. During 2001 it is expected that parts of the oil sector (Servcom) will be privatised at well as the copper and chrome mines. Privatisation of the Savings Bank is also expected to be completed by the end of 2001. The law on the privatisation of between 51 and 76 % of the fixed net operator "Albtelecom" has just been passed by the Parliament.

Although foreign direct investment has increased recently (three-fold compared to previous years) due to the successful privatisations mentioned above, it still remains limited due to structural impediments such as heavy administrative procedures, corruption in the judiciary and the public administration, poor infrastructure and a climate of occasional insecurity, despite considerable progress in consolidating law and order. Financial sector reform has progressed, but further efforts are needed to enhance the legal, regulatory and supervisory framework of the banking sector.

- Implementing the Growth and Poverty Reduction Strategy.
- Developing implementation and monitoring mechanisms for the MTEF.
- Continued efforts in strengthening tax collection and reducing tax evasion.
- Reducing corruption and fraud.
- Boosting the restructuring and privatisation of large-scale enterprises in the strategic sectors.
- Making the National Investment Promotion Agency operational and taking measures to protect foreign investment.
- Implementation of the power sector action plan.

Regional Co-operation

Albania has committed itself to playing a constructive role in the region, be it at the bilateral or multilateral level. The Albanian authorities signed many agreements with neighbouring countries in the period from January 1998 to February 2001. Most of these are co-operation agreements in the educational, cultural and economics spheres. Albania is currently working towards establishing a free Trade Area with FYROM and has increased significantly its co-operation with its EU neighbours in the field of Justice and Home Affairs. In the context of the difficult political situation in neighbouring FYROM, Kosovo and Southern Serbia, Albania has clearly condemned the actions perpetrated by the ethnic Albanian extremist groups, aligning itself with the positions of the international community. In the case of FYROM, it has been pursuing a constructive dialogue both with the authorities and with the ethnic Albanian political leaders. Albania has also improved its relations with FRY through the re-establishment of diplomatic relations. It is actively engaged in the Stability Pact as well as in other regional fora (SECI, SEECP).

- Continuing efforts in co-operation with and the assistance of the international community in combating organised crime and illegal trafficking from and through its territory, by further enhancing the policing of its borders (FRY/Montenegro - Kosovo and FYROM).
- Strengthening co-operation with regional neighbours in the fields of Justice and Home Affairs - as agreed to in the Zagreb Summit - as well as implementing relevant Stability Pact Projects.
- Continuing to use her influence with ethnic Albanian communities in neighbouring countries to promote peace and stability.

2. Operational conclusions

The Council welcomed the Report by the Commission on the work of the EU-Albania High Level Steering Group. It recognised the substantial progress made by Albania and therefore invited the Commission to build on this dynamic with a view to an early presentation of draft negotiation directives for the negotiation of a Stabilisation and Association Agreement with Albania, if possible before the end of the year.

In order to support the ongoing reform process and in view of preparations of the future SAA-negotiations, the Council has agreed that a joint Consultative Task Force with Albania shall be set up, as soon as possible.

B) Bosnia and Herzegovina

For the first time in 10 years, the State government and the government of the Federation of Bosnia and Herzegovina (FBiH) are formed by non-nationalist parties of the multi-ethnic "Alliance for Change", which has expressed its commitment to multi-ethnicity and European integration. In the Republika Srpska (RS), Prime Minister Mladen Ivanic is following a pragmatic course in his support for the "Alliance" at State level. In its relations with the EU, the goal of the new Council of Ministers is to complete the Road Map. Top priorities include i.a. the Election Law, the Civil Service Law, implementation of Property Laws and conditions for sustainable returns.

Still, tensions remain. Bosnia and Herzegovina's (BiH) special problems are exemplified by two current issues: (i) a stand-off with HDZ-inspired "Croat self-rule", mostly in Herzegovina and characterised by systematic intimidation and occasional violence; (ii) the eruption of violence in Trebinje and Banja Luka (RS) as work began on reconstructing Muslim mosques. Acceptance of integration is far from universal.

Despite over US\$ 5 billion in aid, BiH remains one of the poorest countries in Europe (GDP \$972 per capita); its GDP is just over half the pre-war level. Growth rates have declined due to a decline in donors' assistance (2000 +10-12%, 2001 est. +4-5%). Given limited domestic resources, BiH must move from donor-driven to investment-driven growth, but the conditions for attracting foreign direct investment remain poor.

1. Issues needing special attention

Democratic Principles

Progress in fulfilling outstanding Road Map criteria and in advancing the peace process is hampered by nationalist obstruction delaying BiH parliamentary legislative steps. The never-ending battle between those favouring strengthening the State vis-à-vis those safeguarding entity powers is keenly felt at present. The constitutional challenge of the HDZ/CNC-led "Croat self-rule" and setbacks to the peace and reconciliation process in the RS have greatly compounded the State-building process. The Council of Ministers rests on a frail majority and has little time to produce results before the 2002 elections. Adoption of civil service and election laws are important Road Map criteria. The wartime divide between Bosniacs, Serbs and Croats remains deep. Lack of political will and optimism for the future, and widespread corruption, are main reasons for the slow pace of reintegration and reconciliation.

Political influence over the media is common. Recently, the media picture has deteriorated in Croat-controlled areas due to the so-called "Croat self-rule". Strengthening independent media and building the Public Broadcasting System (PBS) are very important. In early May, PBS radio began broadcasting.

- Compliance with the General Framework Agreement for Peace (GFAP) - ICTY, elimination of parallel power structures (especially in the FBiH) etc.

- Adoption of an election law and organisation by the BiH authorities of free and fair elections (next due in 2002).

- Strengthening functional and democratically accountable common institutions, especially at BiH State level, and adoption of the Civil Service Law.

- Strengthening Civil Society.

- Strengthening an independent media landscape.

Human Rights and Rule of Law

In general, there is a slow but steady trend towards an improved human rights situation.

However, there are considerable human rights problems in the country. Attacks on minority returnees, journalists and politicians occur. Discrimination along ethnic lines is common. The educational sector is largely ethnically segregated.

Ensuring that the BiH Constitutional Court's decision on "constituent peoples" is thoroughly implemented is probably the single most important way to strengthen human rights in BiH. The

entity parliamentary Constitutional Commissions are now drafting amendments for the Harmonisation of the entity constitutions with the BiH one. Strengthening the rule of law by establishing a truly independent judiciary continues through the judicial review process.

Continued reform of BiH police forces is necessary.

- Strengthening of the legal system inter alia through sufficient well-trained judges.
- Strengthening the rule of law through judicial reform, police reform and State Border Service (SBS) build-up to fight crime and corruption.
- Strengthening the fight against organised crime, corruption and trafficking in human beings.

Respect for and Protection of Minorities

Until the entity constitutions are amended, making Bosniacs, Serbs, Croats and others constituent peoples throughout BiH, their rights are not fully protected. The Council of Ministers has drafted a law on the rights of ethnic minorities, which will be discussed with the entities and with ethnic minorities prior to submission to parliament. As currently drafted, the law defines 17 ethnic groups as minorities. Each minority would have the right to education in their own language in areas where they constitute a majority, and in areas where they constitute more than three percent they would be entitled to participate in the local authorities.

Regarding return of refugees and displaced persons, minority returns in BiH have doubled in the first three months of 2001 compared with 2000. However, refugee return-related violence occurs. Property law implementation is slow and often obstructed by local authorities. Repossession efficiency rates vary greatly and are on average 13% in the RS and 32% in the Federation. This process must be accelerated.

- Implementing the BiH Constitutional Court's ruling on constituent peoples.
- Ensuring the rights of minorities.
- Strengthening the conditions enabling sustainable refugee returns in line with the Dayton/Paris agreement.

Market Economy Reform

The BiH economy is in dire straits. Living standards are bleak for most citizens. Unemployment averages 40%. The potential risk for increased strikes and growing social unrest is high. The Council of Ministers has few sources of own revenue, relying to some 75% on entity contributions.

The fiscal stance of the entities, particularly of the RS, is a cause for concern. Economic reforms must be pushed vigorously by the Council of Ministers. Creating a single economic area in BiH and removing all inter-entity trade barriers are crucial for economic progress. BiH

must move from donor-driven to growth increasingly relying on domestic forces. Attracting foreign direct investment must be a top priority. The poor investment climate must be improved by easing cumbersome administrative regulations. Private sector development must be encouraged and privatisation accelerated. Increasing compliance with and enforcement of customs and taxation policies are crucial to combat widespread smuggling, fraud and tax evasion. The single BiH standards institute imposed by the High Representative must be approved by the BiH Parliament and adequately funded. Competition and consumer protection legislation must be enacted.

- Continuing ongoing economic reforms, especially the creation of a Single Market, and furthering privatisation.

- Rationalising and reducing the entities' military expenditures.

- Increasing tax collection and independent Council of Ministers revenues.

- Attracting Foreign Direct Investment by appropriate legislation, including Property Laws implementation, Competition and Consumer Protection Law and for a single BiH National Institute of Standards.

Regional Co-operation

Strengthening bilateral relations with Croatia and FRY are crucial prerequisites for the peace process to advance. The recent establishment of Inter-State Councils for Co-operation with Croatia and FRY are good signs that relations are improving. As GFAP signatories, Croatia and FRY have significant responsibilities and influence on BiH developments.

BiH has increasingly become a transit country for illegal migration to the EU. Regional co-operation in the area of justice and home affairs is of the utmost importance. The Sarajevo Joint Declaration of 28 March, adopted by BiH and its neighbours as a follow-up to the Zagreb Summit on regional co-operation in the area of asylum and immigration, must be implemented in earnest.

Securing funding for the further build-up of the State Border Service (SBS) is crucial for BiH to take full control of its borders. On 4 May, a UNMIBH-sponsored agreement on regional co-operation to fight organised crime and trafficking was concluded between the interior ministers of Croatia, FRY and the BiH entities.

- Developing good neighbourly relations, in particular with FRY and Croatia.

- Establishing effective border control, including adoption of the Law on the State Border to fight illegal migration, in line with the Sarajevo Declaration of 28 March.

Compliance with International Obligations and Peace Agreements

Five and a half years after the signing of the GFAP, a massive international involvement in BiH is still needed for the peace implementation process to advance. Despite efforts by the local governments, BiH is still far from being a viable State with sustainable structures that can take sole ownership for the implementation of the Dayton Agreement. Thanks to efforts by the High Representative W. Petritsch and other internationals, which make up for the lack of political will in BiH, the peace process inches forward. The so-called "Croat self-rule" is an illegal parallel structure that must be eliminated. ICTY co-operation is dismal, particularly as regards the RS. No arrests of persons indicted for war crimes (PIFWC)s have been initiated by RS authorities. The draft RS law on co-operation with ICTY must be accompanied by swift action.

- Further efforts to fully comply with the Dayton/Paris agreement.
- Continued efforts towards full co-operation with the ICTY, particular as regards RS.

2. Operational conclusions

The Council expressed its appreciation for the efforts by the new Council of Ministers in BiH to move forward on the path towards European integration. It recalled that the Zagreb Summit called on BiH to fulfil the EU Road Map by the middle of 2001, so that the Commission could undertake a feasibility study as the next step in the Stabilisation and Association process. The Council looked forward to receiving a report from the Commission on the state of completion of the Road Map.

C) Croatia

Croatia is overall a stable democracy and evident progress has been made in the reform process since the change of government in January 2000. Constitutional reform and a clearer re-balancing of institutional powers were important achievements. The authorities are still confronted by structural problems and the consequences of the relative isolation of the economic system in the past. Further efforts are needed to meet the challenges of the transition process and to fully implement the ambitious reform agenda.

Croatia is one of the economically most developed countries of the region (GDP/capita estimated at \$ 4,230 in 2000). After a short recession, GDP started to grow again in the last quarter of 1999, albeit at modest levels and owing to favourable external factors. The overall macroeconomic situation is encouraging, with positive growth in 2000 (3.7% with respect to the previous year), relatively low inflation (4.5% at end year), stable exchange rate and a comfortable current account position expected for 2001.

1. Issues needing special attention

Democratic Principles

The government has been making efforts to enhance political freedoms and transform Croatia into a liberal and more stable democracy. The process of effective decentralisation and strengthening of local government has started and some devolution of powers to the local level formulated in a new law will enter into force on 1 July. Several other parts of the necessary reforms are awaiting decision. A new election law has been passed which provides for democratic elections. However, improvements are deemed necessary regarding representation and participation of minorities. Parliament has passed a new law on the HRT, while the new law on Telecommunications, which will be an important part of the privatisation process, is presently under Parliamentary procedure. The transformation of HRT into a public service broadcaster has however not yet happened and no final decision has been taken on privatising the remaining State-owned press (Vjesnik and Slobodna Dalmacija). Privatisation of the 3rd channel, as recommended by the Council of Europe and the OSCE, should take place in full transparency.

- Pursuing an effective decentralisation and strengthening of local government.
- Improving the procedures for implementation of the provisions in the new election law for minority representation.
- Continuing the reform of the broadcast media with the final adoption of the Law on Telecommunications, including the privatisation of the 3rd TV channel in full transparency.

Human Rights and Rule of Law

The Government of Croatia has initiated a substantial reform of the legal framework governing the democratic institutions. These efforts need to be further pursued. The necessary reforms should include both extensive legislative changes and an administrative overhaul of the judicial system. As for corruption, a decision has been taken to establish an independent anti-corruption agency (USKOK), but actual implementation is pending.

- Pursuing substantial reform of the judiciary to underpin the democratic process.
- Implementing the government's commitment to fight corruption through concrete action.

Respect for and Protection of Minorities

Rights and freedoms are in general respected, but there is still room for improvement as regards rights of persons belonging to national minorities. The already prolonged deadline (May 2001) for a new "Constitutional Law on the Protection of Human Rights and Fundamental Freedoms and on the Protection of the Rights of Ethnic and National Communities and Minorities" has expired, without any evidence that a proposal is about to be presented to Parliament. The government recently announced a new and more decisive policy on refugee returns (the 'Knin conclusions'). In addition to these efforts, steps still need to be taken to ensure continuous and sustainable refugee return in the war-affected areas. The unreformed legal regime of repossession of property, including the issue of lost occupancy and tenancy rights, remains a significant obstacle. Further action is required to ensure that evictions take place in cases of multiple and illegal occupancy. The OSCE has outlined the relevant decisions on legislative and administrative changes that need to be taken to achieve a sustainable refugee return.

- Adoption of the new "Constitutional Law on the Protection of Human Rights and Fundamental Freedoms and on the Protection of the Rights of Ethnic and National Communities and Minorities"
- Fully implementing the refugee return process. This includes continued constructive dialogue and co-operation with the Bosnia and Herzegovina and FRY authorities. Continued efforts are needed on promoting return, creating sustainable conditions for it, securing repossessions and solving the problem of ineffective Housing Commissions, and providing alternative accommodation.

Market Economy Reform

Croatia has a solid industrial base, a qualified and educated workforce and areas with great potential for development like tourism. The consolidation of the banking sector continues and the confidence of banks and depositors seems to be returning. A new Central Bank law has been adopted recently which corresponds to international standards and gives the Central Bank wider authority and independence. A mixture of slow economic growth over the past years, dragging restructuring and modernisation of the economy and wage increases above productivity gains have resulted in high and rising unemployment (reaching a rate of 22.9% in March 2001). More efforts are needed to eliminate administrative obstacles and simplify bureaucratic procedures, which still hamper private sector development. Reform in this area is a necessary prerequisite for attracting foreign direct investment on a larger scale. A fundamental restructuring is necessary to obtain a market economy with a slimmed-down, efficient, decentralised public sector. The necessary reforms required with a view to the implementation of the SAA within the economic policy sphere will require a particular effort. Positive macroeconomic developments will depend greatly on the pursuance of a judicious combination of fiscal adjustment, wage discipline and structural reforms in the context of continued exchange rate stability, as well as on strict obedience to the reform programme

agreed with the IMF and the World Bank. On 19 March 2001, a Stand-by Arrangement (SBA) with the IMF was approved, which provides an important framework of economic policy-making and monitoring in this respect.

- Pursuing a stable and sustainable fiscal policy including a reduction of the public wage bill.
- Streamlining the large public sector including privatisation.
- Improving the legal framework and creating the conditions for private sector development, in particular the tourist sector.
- Strengthening the pension and health care systems.
- Enforcing active employment measures (training, education).

Regional Co-operation

Croatia has a major role to play in the durable stabilisation of the region. Relations with Bosnia and Herzegovina have come to the forefront, and the government of Croatia has urged the Bosnian Croats to look for solutions within the constitutional and institutional framework of Bosnia and Herzegovina. Contacts between government officials and their Yugoslav counterparts are generally positive, but the dialogue with the FRY needs to be further enhanced. Regional co-operation, notably on justice and home affairs, will be an important issue under the Stabilisation and Association Agreement. Recently a co-operation agreement on illegal migration and organised crime has been signed with Bosnia and Herzegovina and the FRY.

- Pursuing efforts to develop fully transparent relations with Bosnia and Herzegovina and to improve relations with FRY to solve outstanding issues, notably Prevlaka.
- Initiating negotiations on a convention on regional co-operation with FYROM, as required under the SA Agreements, as soon as possible.
- Ensuring that expulsions of unwanted aliens take place only to the countries from which they entered Croatia.
- Any challenges or provocation to the common BiH institutions should continue to be condemned.

Compliance with International Obligations and Peace Agreements

Croatia has taken positive steps to co-operate with ICTY, but there is a continued need for full compliance with ICTY obligations. The EU recognises that overall relations between Croatia and Bosnia and Herzegovina have been strengthened. The government of Croatia has also made an earnest effort to reduce its transfers to the Croats in Bosnia and Herzegovina, and to make those transfers more transparent. After disturbing international reports, the government of Croatia is now asking for an audit of its own of last year's transfers, while withholding the transfers included in the State budget for this year.

- Continued efforts need to be undertaken to fully comply with the Dayton/Paris and Erdut agreements.
- Continued efforts towards full co-operation with ICTY, including the transfer to The Hague of Croats indicted for crimes committed on Croatian soil.

- Increasing transparency in relations with neighbouring Bosnia and Herzegovina, in particular in the field of financial transactions to the Bosnian Croats.

2. Operational conclusions

The Council welcomed the initialling of the Stabilisation and Association Agreement with Croatia on 14 May as a historic step in Croatia's integration into European structures. The future signing of the Agreement, and the conclusion of the Interim agreement, will for the first time establish mutual contractual relations between the Union and Croatia. Ahead of the entry into force of the Interim and the Stabilisation and Association Agreements, including their institutional arrangements, the Council agreed that the Joint Consultative Task Force should be maintained and that a Political Dialogue be formalised by means of a Joint Declaration between the EU and Croatia.

D) Federal Republic of Yugoslavia

The Federal Republic of Yugoslavia is today a full participant in, and beneficiary of, the Stabilisation and Association Process. Less than eight months after the "democratic revolution", the Federal and Serbian governments have made progress in many fields although the inherited challenges are still immense. Further to consolidation of political structures, focus has been on reforms aiming at creating the basic conditions for the market economy to operate. The Donors' Conference for the FRY scheduled for 29 June has turned into a clear goal for the authorities. A further priority is resolving the future constitutional relations between Serbia and Montenegro, through an open dialogue and a spirit of compromise, aiming at an agreed redefinition of their relations in a renewed federal framework according to democratic principles. This would also speed up the ongoing reform process. Belgrade has played a crucial and constructive role in resolving the crisis in Southern Serbia. This issue, and the developments in Kosovo, as well as the effects of the tense situation in FYROM, have nevertheless diverted attention from other aspects of the internal reform process.

1. Issues Needing Special attention at Federal/Serbian and Montenegrin Level and in Kosovo

i) At Federal/Serbian Level

Democratic Principles, Human Rights and Rule of Law

Respect for democratic principles, human rights and the rule of law has improved at the policy level. A number of new laws have been adopted, e.g. the amnesty law adopted at the beginning of March. A "Truth Commission" has been set up to promote an open and transparent process in the investigation of crimes. A large number of persons connected to the former regime and under suspicion of abuse of power, economic crime and murder have been arrested or are under investigation. An anti-corruption agency has been created and an anti-corruption law is being prepared. A department for combating organised crime has been set up and the government has proposed the formation of a parliamentary committee to control the State Security Service. A resolution presenting a Code of Conduct for State officials has been passed to Parliament suggesting also the establishment of a control body for the State administration. A new republican penal code has been proposed to Parliament.

But much remains to be implemented, particularly in the field of judicial reform, media independence and rights of persons belonging to national minorities. Around 260 prisoners of ethnic Albanian origin still remain in prisons, some of whom are presumed to be political prisoners. Furthermore, the issue of missing persons from the Kosovo conflict remains to be effectively addressed. Fighting organised crime and corruption is among the most difficult challenges ahead. The three highly political cases (Curuvija, Stambolic and Ibarska highway) remain unsolved. The new republican penal code, which has been proposed to Parliament, will require harmonisation between the federal and republican levels. The fact that the death

penalty is maintained in the new penal code is a matter of deep concern. Improvements and structural reforms at policy level need to be followed up with clear timetables for implementation - particularly in the field of judicial reform.

- Resolving the issue of remaining Kosovo-Albanian prisoners, as well as the issue of missing persons.
- Removing remaining restrictive legislation from the statute books.
- Urgent abolition of the death penalty from the republican penal code.
- Developing an independent media sector and promoting a healthy media climate.

Respect for and Protection of Minorities

The situation of national minorities has improved since September last year. A new law on national minorities is being drafted, as is a law on local self-government. But the situation on the ground for minorities (such as Roma and/or ethnic Albanians) remains difficult in many parts of the country. Efforts should continue with the ambition to place all citizens on an equal footing legally, economically and socially. Also, the commitment by the Serbian government to confidence- building measures in Southern Serbia is highly welcome, as well as their swift implementation.

- Strengthening further the rights of people belonging to national minorities and vigorously tackling discrimination and prejudice against minorities.
- Adopting the Law on local self-government.

Market Economy Reform

The entry of the FRY into the International Financial Institutions is important, as is the temporary and exceptional access to IDA resources granted by the World Bank. A stand-by arrangement with the IMF is being finalised. Progress has been made in restoring macroeconomic stability and starting the process of transformation from a command economy to a modern market economy. Positive steps have been the adoption of new employment laws, a law on extraordinary taxation of revenues and on properties acquired improperly during the Milosevic era, as well as a new law on privatisation. Some progress has also been made in the fiscal sphere, most notably with a first attempt at budget consolidation and tax simplification. However, FRY transition has just started and the reform agenda remains huge. Further progress will be necessary in particular in:

- the rationalisation of public expenditures, including the reduction of military expenditure;
- the creation of a legislative, institutional and policy framework conducive to the development of the private sector;
- the privatisation of socially owned companies and State companies;
- the adoption of a law on foreign investment, guaranteeing the rights of all investors;
- the enhancement of public administration (legal framework, accountability, reduction of discretion in administrative decision-making, etc);
- fighting corruption.

Regional Co-operation

Diplomatic relations have been established with all neighbouring countries and regional co-operation has significantly improved. Belgrade is developing contacts with the BiH-level institutions in Sarajevo, while continuing to develop its special links with Republika Srpska. More recently, Ministers of the Interior from the FRY, Croatia and BiH signed an agreement on co-operation in the area of organised crime and illegal migration. The resolution of outstanding refugee issues remains to be effectively addressed. In relations with Croatia the outstanding regional issue of Prevlaka awaits settlement.

- Undertaking at regional level co-ordinated efforts to resolve refugee issues relating to property rights, and /or economic and social reintegration for those wishing to return by their free will.
- Giving full support to the Dayton process in relations with BiH and giving privilege to the common BiH state institutions. Any illegal challenges or provocation to the common BiH institutions must be clearly condemned.
- Pursuing regional co-operation and reconciliation e.g. within the framework of the Stability Pact, the SEECP and other relevant fora. This includes the resolution of outstanding regional issues, such as Prevlaka.

Compliance with International Obligations and Peace Agreements

A new atmosphere of dialogue characterises the FRY's relations with regional and international interlocutors. FRY has taken a more co-operative stance towards the ICTY. Positive measures have already been taken, such as the arrest and transfer of one indictee as well as the arrest of former President Milosevic. Much remains to be done. The new government has to meet all its international obligations and should continue on the path towards full co-operation with ICTY.

It is also crucial that Belgrade's positive dialogue with UNMIK continues, in order to ensure the participation of Kosovo Serbs in Kosovo society, including in Kosovo-wide elections.

- Undertaking further efforts to fully comply with the Dayton/Paris and Erdut agreements, including efforts towards full co-operation with ICTY. This entails full compliance with UN Security Council Resolution 827, supplemented by the rapid adoption of the appropriate legal framework. Practical steps need to be taken to preserve and provide ICTY with access to evidence and further co-operation on the hand-over of indictees.
- Ensuring a genuine commitment to UNSC resolution 1244 and a continuing active and structured relationship with UNMIK.

ii) At Montenegrin Level

Democratic principles, Human Rights and Rule of Law

In general there is continued respect for democratic principles, human rights and rule of law. The commitment to reform in Montenegro is strong, this has so far resulted in concrete reform measures in the economic sphere. However, much of the political energy in Montenegro has been consumed by the unsettled relations within the Yugoslav federation and the reform process in many other areas remains to be converted into concrete measures. Several draft laws reforming the judiciary and the public sector await adoption, such as the laws on public prosecutors, on courts and in the municipal area. Transparency within the public sector remains to be improved, such as measures aimed good governance, and the police is disproportionately large and unreformed. Furthermore, some questions remain concerning media independence and standards.

- Enacting draft laws concerning the judiciary, the municipal level, aiming at reform, transparency and good governance.
- Initiating thorough reform of the police.
- Assuring media independence in accordance with international standards.

Respect for and Protection of Minorities

The constitutional provisions for minorities are good and the practice is generally functioning satisfactorily.

- Vigorously tackling non-official discrimination and prejudice against minorities.

Market Economy Reforms

Montenegro's macroeconomic situation had steadily deteriorated during a decade of gradual dissolution of the Socialist Federal Republic of Yugoslavia, disruption of trade patterns, wars in the region and economic decline in the larger Serbian market, and the outbreak of the Kosovo crisis.

The Montenegrin authorities moved towards a more independent policy stance towards the end of 2000, inter alia unilaterally adopting the D-mark/€ as sole legal tender. Macroeconomic stability has been broadly maintained, but mostly due to large inflows of foreign grants, covering the fiscal deficit of the Republican budget. On the structural side, various reform measures have been undertaken in the area of public finance (improvement in accounting standards, adoption of an organic budget law and measures to enhance revenue collection), as well as in the monetary area (central bank law). These steps were largely enforced through conditionality attached to the exceptional Community financial assistance provided in 2000.

Further progress is necessary, particularly in:

- further restructuring of public finances, most notably through the introduction of a Treasury system to improve expenditure control;
- promoting the privatisation process in a transparent manner;
- enhancing further reforms of the banking sector;
- supporting small and medium-sized enterprises;
- combating corruption and organised crime, smuggling and trafficking;

iii) Kosovo

The international community is committed to the full implementation of UNSCR 1244. UNMIK and KFOR are working towards establishing a peaceful, multi-ethnic, multi-cultural and democratic Kosovo. In this context, the adoption of the regulation concerning the constitutional framework for provisional self-government in Kosovo is an important step in the implementation of UNSCR 1244. It will provide the basis for Kosovo-wide elections to be held on 17 November. The further development of co-operative relations between Belgrade and UNMIK will also be a priority for building confidence among the Kosovo-Serb community, which should assist in the organisation of Kosovo-wide elections.

The establishment of a secure environment for all the people of Kosovo remains a priority. More improvements must be made in respecting human rights as well as in strengthening the rule of law. In particular, the proper functioning of Kosovo's judicial system has to be ensured.

Much has been achieved in establishing and developing a market economy, under the guidance of EU pillar of UNMIK. However, private investment is still lacking due to insecurity

and ownership problems and future status. In the economic domain, private sector development including privatisation is a key priority. To this extent, rapid progress is needed in creating or completing the essential legal and institutional basis.

2. Operational conclusions

The Council welcomed the important progress achieved by the FRY in consolidating democracy and in promoting the necessary economic and legal reforms, including its efforts to continue on the path towards full co-operation with ICTY. Recalling the perspective as outlined at the Zagreb Summit, the Council agreed to hold the first meeting of the EU-FRY Consultative Task Force, if possible by the end of July, as a first step towards a Stabilisation and Association Agreement. The Council looked forward to a successful Donors' Conference on 29 June.

E) Former Yugoslav Republic of Macedonia

The political situation is tense following the actions of the ethnic Albanian extremists of the "National Liberation Army" which started in March 2001. As a consequence, inter-ethnic relations have deteriorated considerably in the last few months, and it has become obvious that this is the single most important issue facing the country. Thus, a Government of National Unity has been established to overcome the crisis, to engage in an effective inter-ethnic dialogue and to address overall reforms in line with the Stabilisation and Association Agreement (SAA), including legitimate concerns over the rights and status of minorities. As a result of the visit of High Representative Solana to Skopje on 28-29 May, the four party leaders committed themselves to achieving substantial progress on the President Trajkovski reform agenda by June 15.

Macroeconomic developments were encouraging in 2000, as real GDP grew by 5.1%. FYROM made progress with economic reforms and institution-building. The nation is classified as a lower/middle income country and GDP/capita stood at USD 1885 in 2000. In late 2000 macroeconomic policies started to slip and additional military expenditure due to the crisis will burden government finances while structural reforms, including privatisation, appear to be stalling.

1. Issues needing special attention

Democratic Principles

Democratic principles are generally respected, and the democratic process functions normally overall. However, inter-ethnic tensions have increased dramatically in the current crisis. The enhanced inter-ethnic dialogue has been established to make speedy progress in the reform process, e.g. to strengthen local self-government and the integration of under-represented ethnic groups into the administration. There are shortcomings in the Law on Local Elections and the role of the State Election Commission is undefined. The new broader coalition government has, however, a reform of the election law including the election commissions high on its agenda. Lack of participation of MPs in Parliamentary meetings is causing deliberate delays in adoption of important legislation. The media landscape gives room for freedom of expression, but the State-funded media are in the control of the parties in power on an alternate basis and there has been no attempt to transform the State broadcasting company into a "public service".

- Continuing inter-ethnic dialogue at institutional and civic level on necessary reforms (i.a. social and non-governmental organisations, local government, religious leaders and business).

- Developing an appropriate election process including amendment of the Law on Elections to clarify the role of the State Election Commission and the financing of elections. Development of civic education on the conduct of elections;

- Clarifying the status of the Broadcasting Council and its independence from government and strengthening its legal position. A plan should be developed to transform the State broadcaster into a "public service broadcaster".

- Adoption of 3rd Channel in Albanian Languages;

- Adoption of the new Media Law in conformity with international standards.

Human Rights and Rule of Law

Human rights are generally being respected, but there are shortcomings in several areas: the independence of the judicial system needs further consolidation. Many international conventions have been ratified, but need now to be implemented. Impartiality on the part of the police and tax authorities should be ensured. Prison conditions need to be improved. The role and responsibilities of the law enforcement authorities need to be clarified.

- Completing the current process of reform of the judiciary.

- Implementation of the Public Administration Reform.

- Strengthening institutional capacity to deal with corruption, cigarette smuggling, money laundering and international organised crime.

- Structural reform and training of the law enforcement authorities.

- Facilitating and enabling the return of refugees and internally displaced persons, ensuring right conditions, including reconstruction of houses in areas affected by the conflict.

Respect for and Protection of Minorities

Inter-ethnic relations continue to be the single most important issue. The adoption of a new law on education in July 2000 was a major improvement in regard to higher education in Albania, but secondary education in Albanian still remains a concern. The Roma continue to be the most disadvantaged group from a socio-economic point of view.

- Providing a clear timetable to address, in the course of this year, legitimate concerns over the status of minorities and their ability to play a full role in the political, economic and administrative life of the country by recognising the multi-ethnic nature of the country.

- Proceeding with the political dialogue on ethnic issues (inter alia local self-government reform, integration of minorities into the public administration including in particular the police as well as the army, use of minority languages in the courts and public authorities, notably the Parliament.

- Undertaking a census of the population in consultation with the international community, in line with international standards.

- Ensuring the opening in October of the South East Europe University in Tetovo.

Market Economy Reform

In 2000, FYROM signed agreements with the IMF and the World Bank on a new economic programme that could be supported by credits from the International Financial Institutions (IFI). However, the IMF is currently revising the programme in the light of severe economic policy slippages and the recent crisis in the country, which will put a strain on government finances. Progress with new legislation, notably banking and insurance legislation, as well as privatisation, was encouraging in 2000, but the reform pace is currently slowing down, posing a risk to the medium and longer-term growth prospects. The privatisation process, notably

regarding large loss-making enterprises, should be strengthened and made more transparent. The closer economic links with the European Union in the context of the SAA and the unilateral trade measures in favour of FYROM provide an opportunity to strengthen economic transition. However, only a minor range of FYROM products is currently competitive in the EU market.

- Efforts to maintain economic equilibrium and a satisfactory track record on economic policy measures agreed with IFIs.
- Restructuring of public finances, completion of the privatisation process, and compliance with IFIs' conditionality, most notably with regard to selling or closing State-owned loss-making enterprises.
- Promotion of competitiveness through market-based enterprise restructuring, development of small and medium sized enterprises.
- Taking measures to stimulate domestic and inward investments and further reforms of banking and insurance sectors.

Regional Co-operation

FYROM is very active in strengthening regional co-operation. It has taken important steps by entering into bilateral free trade agreements (FTAs) with its neighbours, and furthering a network of FTAs including through the Stability Pact. It has also been actively encouraging improved regional co-operation within the framework of the SEECP. The Government is aware of the problem of organised crime, smuggling of arms, cigarettes and drugs, and trafficking in women. Regional co-operation, notably on justice and home affairs, will be an important issue under the Stabilisation and Association Agreement as well.

- Starting negotiations with Croatia, as soon as possible, on a convention on regional co-operation as required under the Stabilisation and Association Agreement.
- Continuing to enter into bilateral free trade agreements with neighbouring countries to establish Free Trade Areas, thus contributing to the creation of a network of Free Trade Agreements.
- Giving priority to addressing problems of illegal migration and trafficking in human beings, preferably in co-operation with neighbouring countries, for instance through signing up to the agreement on illegal migration and organised crime recently approved by Croatia, Bosnia and Herzegovina and the FRY.

2. Operational conclusions

The Council welcomed the signing of the Stabilisation and Association Agreement with FYROM on 9 April and the entry into force of the Interim Agreement on 1 June. It called upon all political leaders to rapidly achieve concrete and substantial results on inter-ethnic dialogue and to make further progress on overall reforms, thereby accelerating FYROM's progress along the road to Europe under the Stabilisation and Association process.

VI. Conclusions

Conditionality in all its guises is at the heart of the Stabilisation and Association process, as confirmed by the GAC conclusions of 9 April 2001. The establishment of a substantive review mechanism, based on a report prepared by the Commission, has provided the means to assess each country's performance and respect for the conditions of the Stabilisation and

Association process. It allows the EU to assist the countries to progress at their own pace, in accordance with the operational conclusions as set out for each country above.

The above country assessments reflect priorities identified and recommendations on action to be taken for Albania, Bosnia and Herzegovina, Croatia, FYROM and FRY. The EU will expect each country to pay special attention to and to devote the necessary resources to the priority areas for action identified in these reviews.

The present report on the Stabilisation and Association Process represents a first political review. A full review, including an assessment of the efficiency of the Stabilisation and Association process instruments, will be undertaken before the end of this year, and then on an annual basis. Notwithstanding the annual review, the Council will, on a continuous basis, follow overall developments in the countries concerned.