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ON

CYPRUS'S

PROGRESS TOWARDS ACCESSION

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A. Introduction

a) Preface

In Agenda 2000, the Commission said it would report regularly to the European Council on progress made by each of the candidate countries of Central and Eastern Europe with preparations for membership, and that it would submit its first Report at the end of 1998.

The Luxembourg European Council decided that:

“From the end of 1998, the Commission will make Regular Reports to the Council, together with any necessary recommendations for opening bilateral intergovernmental conferences, reviewing the progress of each Central and Eastern European applicant State towards accession in the light of the Copenhagen criteria, in particular the rate at which it is adopting the Union *acquis* [...] The Commission’s reports will serve as the basis for taking, in the Council context, the necessary decisions on the conduct of the accession negotiations or their extension to other applicants. In that context, the Commission will continue to follow the method adopted by Agenda 2000 in evaluating applicant States’ ability to meet the economic criteria and fulfil the obligations deriving from accession.”

On this basis, the Commission presented a first series of Regular Reports in October 1998, a second in October 1999, a third in November 2000, and a fourth in November 2001.

In its 2001 Enlargement Strategy Paper, which accompanied the 2001 Regular Reports, the Commission indicated that, given the pace of negotiations and the progress made so far, the Commission should be able to make recommendations on those candidate countries ready for accession on the basis of its 2002 Regular Reports. At its meeting in Seville in June 2001, the European Council concluded that “in order to enable the European Council to be held in the coming autumn to decide which will be the candidate countries with which negotiations can be concluded at the end of 2002, [...] the Commission will have to draft appropriate recommendations in the light of the Regular Reports.” The Commission has prepared this series of Regular Reports with a view to the Brussels European Council in autumn 2002.

The structure followed for this Regular Report is largely the same as that used for the 2000 and 2001 Regular Reports. In line with previous Regular Reports, the present Report:

- describes the relations between Cyprus and the Union, in particular in the framework of the Association Agreement;
- analyses the situation in respect of the political criteria set by the 1993 Copenhagen European Council (democracy, rule of law, human rights, protection of minorities);
- assesses Cyprus’s situation and prospects in respect of the economic criteria defined by the Copenhagen European Council (a functioning market economy and the capacity to cope with competitive pressures and market forces within the Union);

- addresses the question of Cyprus's capacity to assume the obligations of membership, that is, the *acquis* as expressed in the Treaties, the secondary legislation, and the policies of the Union. In this part, special attention is paid to nuclear safety standards, which were emphasised by the Cologne and Helsinki European Councils. This part includes not only the alignment of legislation, but also the development of the judicial and administrative capacity necessary to implement and enforce the *acquis*. The European Council stressed the importance of this latter aspect at its meeting in Madrid in 1995 and on a number of subsequent occasions, most recently at Seville in June 2002. At Madrid, the European Council stressed that the candidate countries must adjust their administrative structures, so as to create the conditions for the harmonious integration of these States. The Seville European Council also stressed how important it was that candidate countries should continue to make progress with the implementation and effective application of the *acquis*, and added that candidate countries must take all necessary measures to bring their administrative and judicial capacity up to the required level.

This Report takes into consideration progress since the 2001 Regular Report. It covers the period until 15 September 2002. In some particular cases, however, measures taken after that date are mentioned. It looks at whether planned reforms, referred to in the 2001 Regular Report, have been carried out, and examines new initiatives. In addition, this Report provides global assessment of the overall situation for each of the aspects under consideration, setting out for each of them the main steps still to be taken by Cyprus in preparing for accession.

Furthermore, in view of the fact that the 2002 Regular Reports will provide the basis on which the Commission will formulate its recommendations as to which countries are ready to conclude negotiations, this Report includes an evaluation of Cyprus's track record since the 1998 Regular Report. For the economic criteria the track record covers the period since 1997 and the report also provides a dynamic, forward-looking evaluation of Cyprus's economic performance.

Finally, for each of the negotiating chapters, this Report provides a summary evaluation of the extent to which commitments made in the negotiations have been implemented, as well as an overview of transitional arrangements that have been granted. The commitments made by each country reflect the result of the accession negotiations, and, in accordance with the principle of differentiation underlying the negotiation process, may differ between countries. Where negotiating countries have committed themselves to completing specific measures by the time of accession, the Commission assesses the relevant preparatory processes. For chapters on which the accession negotiations continue, and final commitments remain to be defined, an indicative assessment is given of the state of implementation of the commitments that have been made to date.

The Report includes a separate section examining the extent to which Cyprus has addressed the Accession Partnership priorities. This section also assesses the progress Cyprus has made in implementing the measures set out in the Action Plan for strengthening administrative and judicial capacity that the Commission developed with each negotiating country in the spring of 2002.

As has been the case in previous Reports, "progress" has been measured on the basis of decisions actually taken, legislation actually adopted, international conventions actually ratified (with due attention being given to implementation), and measures actually

implemented. As a matter of principle, legislation or measures which are in various stages of either preparation or Parliamentary approval have not been taken into account. This approach ensures equal treatment for all the candidate countries and permits an objective assessment of each country in terms of their concrete progress in preparing for accession.

The Report draws on numerous sources of information. The candidate countries have been invited to provide information on progress made in preparations for membership since the publication of the last Regular Report. The information each of the candidate countries has provided within the framework of the Association Agreement and the negotiations, the National Programmes for the Adoption of the *Acquis* where they are available, as well as the process of developing the Action Plans, and various peer reviews that have taken place to assess candidate countries' administrative capacity in a number of areas, have served as additional sources. Council deliberations and European Parliament reports and resolutions¹ have been taken into account in the preparations. The Commission has also drawn on assessments made by various international organisations, and in particular the contributions of the Council of Europe, the OSCE and the international financial institutions, as well as those of non-governmental organisations.

b) Relations between the European Union and Cyprus

Recent developments under the Association Agreement, including bilateral trade

Relations between the EU and Cyprus are based on the Association Agreement of 1973, which contains arrangements on trade and customs matters, and the Accession Partnership (AP) of March 2000². Cyprus has continued to implement the Association Agreement correctly.

The Association Council did not meet over the reporting period. The last meeting was held in May 2001 (see Regular Report 2001).

The *EU-Cyprus Joint Parliamentary Committee*, held its 20th meeting in October 2001 in Brussels and its 21st meeting in May 2002 in Nicosia. Both meetings underlined that Cyprus had made good progress in the accession negotiations. Solution of the Cyprus problem before Cyprus's accession to the Union would be beneficial for all parties but was not a precondition for EU membership. The 21st meeting also discussed the Euro-Mediterranean Partnership, the future of Europe, and the protection of Cyprus's environment and the cultural heritage.

In December 2001, the Association Council adopted a decision setting up a Joint Consultative Committee between the Committee of the Regions and the Cypriot Liaison Committee for Co-operation with the Committee of the Regions. A delegation of the Economic and Social Committee visited Cyprus in March 2002 and issued a report on the economic and social situation in the Republic of Cyprus and in the North.

¹ For the European Parliament the *rapporteurs* are Elmar Brok and Jacques Poos.

² Council Decision (EC) No. 248/2000 of 20 March 2000 on the principles, priorities, intermediate objectives and conditions contained in the Accession Partnership with the Republic of Cyprus, which entered into force on 1 April 2000.

A decision on the conclusion of an Additional Protocol to the Association Agreement concerning bilateral concessions relating to trade in fish and fishery products entered into force in January 2002.

In February 2002, the Council adopted a mandate authorising the Commission to open negotiations with Cyprus on improving agricultural trade concessions. Liberalisation proposals were presented to Cyprus along the lines of the approach adopted for the countries of Central and Eastern Europe in the “double profit” negotiations.

As regards EC-Cyprus trade in 2001, it amounted to € 2.6 billion of exports to the EC (55.5% of total) and € 0.9 billion of imports from the EC (49% of total). The current account deficit stands at € 1.7 billion. Concerning trade by products, transport equipment represents the largest sector for EC imports from Cyprus followed by agriculture, machinery and textiles. As regards exports to Cyprus they consist mainly of transport equipment and machinery followed by agriculture and chemical products.

In March 2002, in response to protectionist measures taken by the US, which greatly restricted access to their market and created the risk of considerable trade diversion, the EU initiated provisional safeguard measures, with erga omnes effect, on imports of certain steel products. The measures were partly confirmed in September 2002.

Accession Partnership

A revised Accession Partnership entered into force in February 2002. Its implementation is reviewed in Part D of this Report.

Action Plan for reinforcing administrative and judicial capacity

As announced in the Commission's 2001 Enlargement Strategy, in spring 2002 the Commission and Cyprus jointly developed an Action Plan to strengthen Cyprus's administrative and judicial capacity, on which common understanding was reached in April. The revised Accession Partnership that was adopted in February has served as the point of departure for this exercise.

The purpose of this Action Plan is to jointly identify jointly the next steps required for Cyprus to achieve an adequate level of administrative and judicial capacity by the time of accession, and ensure that all necessary measures in this regard are taken, providing Cyprus with targeted assistance in areas that are essential for the functioning of an enlarged Union. As such, the Action Plan is a key tool for meeting the common objective of the EU and Cyprus, i.e. to ensure that Cyprus's preparations for accession take place as effectively as possible within the planned timeframe.

The implementation of the Action Plan is reviewed in Part D of this Report.

National Programme for the Adoption of the Acquis

Cyprus has not updated its National Plan for the Adoption of the Acquis (NPAA) since August 2001.

Community Assistance

In May 2000, following the expiry of the 4th Financial Protocol at the end of 1999, the Council adopted a Regulation laying down the conditions for Community assistance to Cyprus. It provides for pre-accession aid to Cyprus for the period 2000-2004 amounting to € 57 million, to be used mainly for strengthening of institutional capacity, as well as for participation in Community programmes. One third of the funds should be used to finance bi-communal projects (activities to contribute to the reconciliation of the two Cypriot communities). The Regulation also provides for Cyprus's participation in MEDA regional programmes. In addition, Cyprus is eligible for the EIB pre-accession facility and for the € 6.425 billion EIB facility for Mediterranean countries.

The **2000** pre-accession allocation (€ 9 million) was earmarked for activities in the following sectors: taxation, customs, Schengen Information System, administrative co-operation, bi-communal projects, and participation in the Community programmes on education (Socrates, Leonardo, Youth).

The **2001** allocation (€ 11.5 million) went to the following fields: environment (in particular waste water treatment), the internal market (more specifically VAT and customs harmonisation, accreditation and standardisation), the social sector, administrative co-operation and participation in Community programmes. Three projects were also programmed to support reconciliation between the two Cypriot communities.

The main projects planned for **2002** (€ 11.5 million), apart from bi-communal projects, concern free movement of goods and the internal market (standardisation, telecommunications and customs), preparations for EU policies (CAP enforcement, preparations for the Structural Funds), maritime transport, justice and home affairs (drugs), statistics, administrative co-operation and participation in Community programmes.

As mentioned above several **bi-communal projects** have been programmed under the 2000, 2001 and 2002 budgets. The EC is contributing € 7 million to urban regeneration and historical preservation schemes under the Nicosia Master Plan. This Plan aims to preserve the cultural and historical heritage of the walled city, so as to provide a new impetus for private investments and improve the urban fabric of the city. The EC projects will be implemented through the executing agency of the United Nations Development Programme UNOPS (United Nations Office for Project Services), which has been actively involved in the Nicosia Master Plan since 1998. € 0.3 million in EC funds is being used to help to strengthen the links between Greek Cypriot and Turkish Cypriot trade unions and develop their shared interests with a view to accession. A communication strategy (€ 0.4 million) is also focusing on increasing public awareness of and interest in the EU among both Greek and Turkish Cypriot communities. Bi-communal projects in 2002 also include a business support scheme based on co-operation between the chambers of commerce of the two communities.

As regards **Community Programmes**, Cyprus is currently participating in Media II, Life II, the fifth R&D Programme, Socrates, Leonardo, Youth, and the Multi-annual Programme for Enterprises and Entrepreneurship. It also plans to take part in Customs 2000, Save, Altener, Culture 2000, Media Plus and Fiscalis in the near future. Cyprus has also been participating in the activities of the European Environment Agency since 2001.

Twinning

One of the main challenges still facing the candidate countries is the need to strengthen their administrative and judicial capacity to implement and enforce the *acquis*. As of 1998, the European Commission began to mobilise significant human and financial resources to help them with this process, using the mechanism of twinning administrations and agencies. In 2001, the Commission strengthened this emphasis on institution building further, through the launch of the Action Plans for strengthening administrative and judicial capacity.

The twinning process makes the vast body of Member States' expertise available to the candidate countries through the long-term secondment of civil servants and accompanying short-term expert missions and training.

A total of 503 twinning projects were funded by the Community between 1998 and 2001. Between 1998 and 2000, these projects primarily targeted the main priority sectors identified in the Accession Partnerships: agriculture, the environment, public finance, justice and home affairs and preparation for the management of Structural Funds. Since 2000, other important sectors of the *acquis* have also been addressed through twinning, such as social policy, the fight against drugs, transport, and telecommunications regulation. Twinning now covers all sectors pursuant to the *acquis*.

Thanks to the strong support of the EU Member States, 103 twinning partnerships were funded by Phare 1998, involving all the candidate countries and almost all the Member States. These first-generation projects have already come to an end. Under Phare 1999 a further 123 projects are currently being implemented and the programming exercise for Phare 2000 included a further 146 twinning projects. The 2001 programming exercise includes 131 twinning projects embracing all the Phare beneficiary countries, as well as Cyprus and Malta. Under the 2002 programming exercise, 119 twinning projects have already been planned, and approved for implementation. A substantial number of additional twinning projects are planned, and these should be approved and implementation launched before the end of 2002. They include twinning projects identified in the Action Plans for strengthening administrative and judicial capacity in the negotiating countries. It is estimated that around 300 twinning projects are operational throughout the candidate countries at any one time. Furthermore, the candidate countries are being offered a further way of drawing on Member States' expertise through "Twinning light", a mechanism to address carefully- circumscribed projects of limited scope which emerge during the negotiation process as requiring adaptation.

There are currently several twinning projects running in Cyprus in fields including the Structural Funds, state aids, metrology, insurance and asylum.

Negotiations

Since the opening of accession negotiations, substantive discussions on the individual chapters of the *acquis* have started and negotiations on all the chapters (except Chapter 31 – Other) have been launched.

By the end of September 2002 negotiations on the following 28 chapters had been provisionally closed: Free movement of goods, Free movement of persons, Freedom to provide services, Free movement of capital, Company Law, Competition policy,

Fisheries, Transport policy, Taxation, Economic and monetary union, Statistics, Social policy and employment, Energy, Industrial policy, Small and medium-sized enterprises, Science and research, Education and training, Telecommunications and information technologies, Culture and audio-visual policy, Regional policy and co-ordination of structural instruments, Environment, Consumers and health protection, Co-operation in the field of Justice and home affairs, Customs union, External relations, Common foreign and security policy and Financial control. Good progress on the remaining chapters of Agriculture and Budget can be reported.

c) The British Sovereign Base Areas after Cyprus's Accession

During the last year, bilateral meetings between the United Kingdom and the Commission as well as trilateral meetings together with Cyprus have been held. Issues discussed included how Cyprus's accession to the EU would affect the British Sovereign Bases Areas (SBA) on Cyprus, with a view to maintain the special arrangements agreed between the United Kingdom and Cyprus under the Treaty of Establishment of 1960 and to ensure that the Cypriots living and working in the SBA's should have the same treatment, for certain EU policies, as those living and working in the Republic of Cyprus.

B. Criteria for membership

1. Political criteria

Introduction

The political criteria for accession to be met by the candidate countries, as laid down by the Copenhagen European Council in June 1993, stipulate that these countries must have achieved “stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities.”³

The Commission has repeatedly concluded that Cyprus fulfils the Copenhagen political criteria.

In its 2001 Regular Report, the Commission found that:

"Cyprus continues to fulfil the Copenhagen political criteria. Further efforts have been made to prepare the administration for operation within the EU, and the authorities' record on democratic and human rights remains generally good."

The section below provides an assessment of developments in Cyprus, seen from the perspective of the Copenhagen political criteria, including the overall functioning of the country's executive and its judicial system. Such developments are in many ways closely linked to developments regarding Cyprus' ability to implement the *acquis*, in particular in the domain of justice and home affairs. Specific information on the development of Cyprus' ability to implement the *acquis* in the field of justice and home affairs can be found in the relevant section (*Chapter 24 – Cooperation in the field of justice and home affairs*) of part *B.4.1.* of this Report.

Recent developments

No elections have taken place in Cyprus since the last Regular Report. The coalition of the Democratic Rally and the United Democrats has continued to govern the country under the Presidency of Mr Clerides.

On 16 January 2002, Mr Clerides and Mr Denktash, as leaders of their communities, started direct talks under the auspices of the United Nations to reach a political settlement (*see Part B. 2. Prospects for a political settlement*).

³ In the meantime, through the entry into force of the Treaty of Amsterdam in May 1999, the political criteria defined at Copenhagen have been essentially enshrined as a constitutional principle in the Treaty on European Union. Article 6(1) of the consolidated Treaty on European Union reads: "The Union is founded on the principles of liberty, democracy, respect for human rights and fundamental freedoms and the rule of law." Accordingly, Article 49 of the consolidated Treaty stipulates that "Any European State which respects the principles set out in Article 6(1) may apply to become a member of the Union." More recently, these principles were emphasised in the Charter of Fundamental Rights of the European Union, that was proclaimed at the Nice European Council in December 2000.

1.1. Democracy and the rule of law

Cyprus has achieved stability of institutions guaranteeing democracy and the rule of law. This was the conclusion of previous Regular Reports, and has been confirmed by developments over the past year. This section focuses on the most significant developments since the last Regular Report.

The parliament

The Parliament has continued to function in full respect of democratic principles, and has again made considerable efforts to align a substantial amount of legislation with the *acquis*.

The special Committee for European Affairs that was established following the parliamentary elections of May 2001 examines EU-relevant bills and regulations. Upon approval by this Committee, the House can apply a fast-track procedure to adopt them in the plenary. Over the last year, the Cypriot Parliament has made extensive use of this possibility and has adopted the majority of *acquis*-related laws and regulations in this way. To assist the members of the European Affairs Committee in their task, the House has also established a European Affairs Department consisting of legal officers who have received specialised training in European law.

The executive

The institutions of the President and the Council of Ministers, consisting of 11 Ministers, have continued to operate smoothly.

Under the Public Service Law of 1990 civil servants are bound to act according to the law. The power to appoint, promote, transfer, retire and exercise disciplinary control over public officers is vested in the Public Service Commission. A Citizen's Charter assists citizens in exercising their rights vis-à-vis the administration.

The reform of the state public administration is an ongoing process. During the last year the Public Administration and Personnel Service has completed a number of studies to enhance the efficiency and effectiveness of the civil service. Accordingly, 185 additional posts were created in 2001. The Cypriot administration has also introduced in some Ministries an automation system that accelerates access to documentation.

The Chief Negotiator is responsible for EU accession negotiations and co-ordinates the harmonisation process. The pre-accession strategy is implemented by the Planning Bureau, whose staff was reinforced on a temporary basis in summer 2002. There are one or two co-ordinators in each Ministry for both the harmonisation process and the pre-accession strategy. To inform the public at large, the Office of the Chief Negotiator has created an Internet website in which important developments regarding the negotiation and harmonisation process are presented in Greek, Turkish and English.

Within the Law Office, the posts of 20 specialised lawyers working within the European Law Section have been transformed from temporary into permanent posts. In addition, the Attorney-General has assigned experts for the drafting of bills relating to certain highly technical aspects of the *acquis*. In the first five months of 2002, the Law Office completed legal vetting of over 200 pieces of *acquis*-related legislation.

Training has been continuously promoted. From July 2001 to April 2002, the Public Administration and Personnel Service subsidised the participation of officials in various general seminars to improve their technical, management and IT skills. In addition, the Cyprus Academy of Public Administration trains civil servants specifically on European Union issues to deepen understanding of the EU's institutions, structures and policies and their impact on the Cypriot administration after accession. The same is true for the Cyprus Police Academy, that has incorporated in its training programmes modules relating to justice and home affairs and human rights as well as other EU-related matters.

There are no significant developments to report as regards regional and local administration. Cyprus continues to be subdivided into 6 districts with two types of local government, i.e. Municipalities (33) and Community Councils (576), which are mainly financed by government subsidies.

The judicial system

The two-tier structure of the Cypriot judicial system (first instance courts and Supreme Court) has remained in place. Under the Constitution judges are bound to be impartial. They are independent from the other branches of government. Whereas first instance judges are appointed, transferred and promoted by, and are subject to the disciplinary jurisdiction of, the Supreme Council of Judicature (composed of members of the Supreme Court), the Supreme Court judges are appointed by the President. The remuneration and tenure of judges is protected against arbitrary interference by law. The right to fair trial is guaranteed in Article 30 of the Constitution.

The total number of Cypriot judges remains at 84, although in 2001 the judiciary again asked for an increase of the number of District Judges. Parliament has not yet approved the relevant bill, but following the construction of new buildings the Nicosia District Court has increased its capacity and can now house up to 8 new judges.

Two judgments of the European Court of Human Rights of July 2002 found that civil proceedings were not handled in a reasonable time by the District Court of Nicosia between 1986-1997⁴ viz. 1998-1999⁵. The measures to expedite the administration of justice at first instance referred to in the last Regular Report (expansion of powers of District Courts, changes in the rules of civil and criminal procedure, delivery of judgments within 6 months of the conclusion of the hearing) are, however, bearing fruit this year. The number of cases pending at first instance at the end of 2001 has further decreased (71 542 in 2001 as compared to 74 452 in 2000). Further efforts to reduce the length of proceedings are necessary in particular with a view to EU accession. In 2001, the Supreme Court concluded more appeals in civil cases, reducing the number of pending cases to 397 (compared to 418 in 2000). However, as regards criminal cases, the number of appeals filed with the Supreme Court is slightly larger than the number of judgements handed down, and some criminal proceedings had to be invalidated on account of inordinate delay. This shortcoming was also highlighted by the European Court of Human Rights, which concluded in May 2002⁶ that a criminal case that lasted over six years was not handled in a reasonable time at the District Court level.

⁴ Alithia Publishing Company v. Cyprus, Application no. 53594/99 of 11 July 2002.

⁵ Markass Car Hire Ltd. v. Cyprus, Application no. 51591/99 of 2 July 2002.

⁶ Georgiades v. Cyprus, Application no. 50516/99 of 14 May 2002.

During the last year, Cyprus has created 50 new posts of prosecutors at the Law Office of the Republic. They replace the prosecutors of the Police. At the time of writing at least 8 posts have been filled, whilst the selection procedure for the remaining posts is under way.

The training programme established by the Supreme Court in 2000 has continued over the last year. Cypriot judges attended five seminars on, *inter alia*, EU law in general and specialised subjects like European competition and environmental law.

Anti-corruption measures

Cyprus has a comprehensive legal framework against fraud and corruption. As observed in previous Regular Reports, the Penal Code defines a series of offences of official corruption, such as extortion by public officers, abuse of office, or neglect of official duty. In addition, the Prevention of Corruption Law sanctions both public and private corruption. The Public Service Law of 1990 contains special anti-corruption provisions and a corresponding code of conduct allows for compulsory retirement or dismissal after a disciplinary punishment.

The Unit for Combating Money Laundering at the Law Office (*for further details see also Chapter 4 - Free movement of capital*), the Financial Crime Unit of the Police and the Special Investigation Unit at the Department of Customs and Excise are responsible for enforcement. Furthermore, investigation units in the Income Tax and VAT Departments continue to deal with cases of irregularities including fraud. The Attorney General co-ordinates all investigations concerning fraud and corruption. He may also appoint an independent criminal investigator upon a written complaint against a member of the Police Force for an alleged criminal offence.

Cyprus ratified the Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime in 1997. Whereas the Council of Europe Criminal Law Convention on Corruption entered into force in Cyprus in July 2002, ratification of the Civil Law Convention on Corruption that it signed in November 1999 is still outstanding. Cyprus' application to join the OECD Convention on Combating Bribery of Foreign Officials in International Business Transactions is pending (*see also Chapter 24 - Co-operation in the field of Justice and Home Affairs*).

As a member of the Group of States Against Corruption (GRECO) of the Council of Europe, Cyprus received a mission from three experts in December 2000. According to the evaluation report that was adopted and made public in December 2001, Cyprus appeared to belong to the group of GRECO members that are least affected by corruption. However, the report adds that there existed several factors that rendered the country to a certain degree vulnerable. While the authorities appeared to be well aware of the risks and had taken a number of initiatives with a view to tightening up their criminal legislation on corruption, Cyprus still lacks a comprehensive anti-corruption policy in the wider sense as is evidenced by the absence of any regulation on funding of political parties. The report further finds that, although the country could rely on a range of independent and adequately skilled authorities for the fight against corruption, its law-enforcement mechanism does not use sufficiently proactive methods and its intelligence-gathering system has several pitfalls. The report adds that the internal complaints system of the police has not been sufficiently tested in practice and the competence of the Audit

Office is in some respects unduly restricted. In conclusion, GRECO addressed 10 specific recommendations to Cyprus, which it is strongly encouraged to follow up.

1.2. Human rights and the protection of minorities

Cyprus continues to respect human rights and freedoms. This was the conclusion of previous Regular Reports, and has been confirmed over the past year. The following section focuses on the most significant developments since the last Regular Report.

Cyprus has ratified all major *human rights conventions* (see Annex). In early 2002, it acceded to the Optional Protocol to the UN Convention on the Elimination of Discrimination against Women. This allows individuals to submit communications to the international supervisory body after having exhausted local remedies. Cyprus also ratified Protocol No. 12 to the European Convention on Human Rights (ECHR) in April 2002 prohibiting discrimination on any grounds. Cyprus signed Protocol No. 13 to the ECHR concerning the abolition of the death penalty in all circumstances in May 2002.

As observed in previous Regular Reports, any direct or indirect *discrimination* against any person on the grounds of his community, race, religion, language, sex, political or other convictions, national or social descent, birth, colour, wealth, social class, or any ground whatsoever, is prohibited under Article 28(2) of the Cypriot Constitution. Cyprus still needs to ensure full transposition and implementation of the EC anti-discrimination *acquis* based on Article 13 of the EC Treaty (*see Chapter 13 – Social policy and employment*).

The Office of the Ombudsman, whose task is to investigate, report on and make recommendations concerning acts or omissions of the administration, including local authorities, as well as alleged ill-treatment by members of the police, continues to function well. During 2001, the Ombudswoman dealt with 1 331 cases, mainly in the areas of labour and education, immigration and concerning the relationship between public bodies and citizens. Presenting the annual report to Parliament in spring 2002, the Ombudswoman, however, complained that several governmental and local bodies were uncooperative during her investigations and that her suggestions were not applied in full.

Civil and political rights

Civil and political rights continue to be generally respected. *Inter alia*, the procedure for the protection of refugees has been improved, and some progress can be reported as regards those issues that exist due to the Cyprus problem.

The *death penalty* remains in the Cypriot Military Criminal Code for six military offences if committed in times of war. With the signature of Protocol 13 to the ECHR in May 2002 the Cypriot government demonstrated its intention to abolish this provision in the near future.

Torture, inhuman or degrading treatment is prohibited by Cypriot law. Since April 2001 the Attorney General has had the power to appoint special investigators to look into alleged criminal offences by the police force not only upon submission of a written complaint, but also *ex officio*. The Attorney General exercised this right in more than thirty cases in the period from April 2001 to July 2002.

As was noted in the previous Regular Report, the European Court of Human Rights found in two cases⁷, relating to events in 1995 and 1994 respectively, that policemen had gone beyond reasonable use of force against suspects who were Turkish Cypriots. In the period under review, the Government paid the outstanding compensation as ordered by the Court in the second case. As a reaction to both cases, the Attorney-General circulated instructions to the Chief of Police, the Ministry of Justice and Public Order and the Ministry of Interior to acquaint all members of the security forces exercising powers of arrest, detention and interrogation with the two judgments. Despite the Attorney General's remark in his circular that mistreatment of persons within the meaning of Article 3 of the European Convention on Human Rights is a criminal offence under Cypriot law and that there would be no impunity, the responsible authorities have not yet initiated criminal proceedings or taken disciplinary measures against the perpetrators in the Deniczi case, which the Commission notes with concern.

Trafficking in human beings constitutes a criminal offence in Cyprus. In particular, the sale of children and the exploitation of women and children by prostitution are outlawed. The relevant law of 2000 also provides for the appointment of a guardian for the protection of the victim. However, the recruitment of young women, mainly from Eastern Europe, for prostitution has continued during the last year. Three individuals were charged with trafficking under the new law.

The right to liberty is protected by Article 11 of the Constitution. As observed in previous Regular Reports, various remedies exist to challenge the validity of *pre-trial detention*. The bill proposed by the Government in April 2001 with the aim of providing payment of just and reasonable compensation to persons having partially served a term of imprisonment following conviction for a criminal offence, when their conviction is quashed on appeal, is still pending at the time of writing.

Cyprus has continued to upgrade its *prison conditions* during the last year. The renovation of two old wards of a prison is to be completed by the end of 2002. 48 new posts of prison personnel that were created in 2001 have been filled (permanently or temporarily) in the course of 2002. In addition, two new posts of Senior Prison Officers were created during 2002.

According to Article 30(3) of the Constitution, every person has the right to have free *legal aid* where the interests of justice so require and as provided by law. The law for the statutory introduction of legal aid, which includes family law cases was approved in July 2002.

Cyprus amended its *refugee* law in January 2002. Taking over the responsibility of the UNHCR, the newly established Refugee Authority processes *asylum* applications in its own premises in the Migration Department's building complex of the Ministry of Interior. The first interviews with asylum seekers started in March 2002. Interpreters are available for Farsi, Turkish, Arabic, Russian and Serbo-Croat. The Refugee Authority has prepared an informative booklet for applicants, and the eligibility officers receive ongoing training by UNHCR. The land on which a reception centre for refugees is to be built by the end of 2002 has been secured.

⁷ Egmez v. Cyprus of 20 December 2000 and Deniczi vs. Cyprus of 23 May 2001.

In February 2002, the Council of Ministers adopted a comprehensive National Report on the Implementation of the Conclusions of the European and World Conferences against *Racism*. First case law arose under the Cypriot statute implementing the UN Convention on the Elimination of All Forms of Racial Discrimination. An Inter-Ministerial Committee was appointed to monitor the Action Plan contained in the Convention. It focuses on further improvement of the legal framework and suggests additional educational measures. A Cypriot NGO alleged that the immigration services were badly treating foreigners in several cases in spring 2002.

Freedom of speech, which is guaranteed under Article 19 of the Constitution, continues to be generally respected. Independent newspapers and periodicals can voice criticism of the government. Private television and radio stations compete with the stations that are owned by the state.

Article 18 of the Constitution protects the *freedom of religion*. There is no state religion in Cyprus and no law makes any distinction between religions. The freedom to profess a faith and to manifest a religion or belief, in worship, teaching, practice, or observances can be freely exercised in practice.

On 11 July 2002, Parliament fixed the age of consent for both heterosexual and homosexual relationships at 17 years. The new penal law thereby abolishes the previously existing difference in age as regards consent, depending on *sexual orientation*.

Article 21 of the Constitution affords to every person the right to freedom of *peaceful assembly and of association* with others. The Government continues to respect these rights in practice.

There are various *non-governmental organisations (NGOs)* in Cyprus that promote human rights education and awareness among the public at large. The Government supports and subsidises their programmes and activities. A specialised NGO runs a shelter for battered women in Nicosia and a fund for legal aid to victims of domestic violence.

Some progress has been made in tackling the specific issues in relation to various civil and political rights that were noted in the previous report as existing due to the Cyprus problem.

The restrictions to the *right to marry* for Turkish Cypriots living in the south have been abolished after the European Court of Human Rights, in September 2001, had declared an application of a Turkish Cypriot admissible under various Articles of the ECHR⁸. A law of May 2002 now allows civil marriages to be celebrated by mayors as marriage officers irrespective of the faith of one or both parties involved, superseding previous legal provisions according to which only judges of the Turkish Communal Courts could act as marriage officers in these cases.

The Turkish Cypriots living in the government controlled areas cannot exercise their *right to vote*. Participation in national elections would entail a constitutional revision. A

⁸ Selim v. Cyprus, Application no. 47293/99 of 16 July 2002. The Court struck the case out of its list since the applicant and the Government reached a friendly settlement in February 2002 and the Government notified the new law in May 2002 to the Court.

bill according to which Turkish Cypriots would be allowed to participate in municipal and communal elections was tabled in Parliament in November 2001, but it has not yet been adopted.

Economic, social and cultural rights

As regards *equal opportunities*, Cypriot women have the same legal status as men (*for further detail see chapter 13 – Social Policy and Employment*). However, under-representation of women in political life persists. Of the current 56 Members of Parliament, only six are women. There is no female Minister in the Government. Since April 2002, the National Machinery for Women's Rights has organised a training programme on Gender Mainstreaming for the gender focal points and high-ranking officials from various Ministries, with the aim of creating awareness among officers and decision makers concerning gender equality issues.

Children's rights are taken seriously. Free education is available at all levels until the age of 18. Education is compulsory up to the age of 15, and children may not be employed in the industrial sector below the age of 16. Labour inspectors enforce the law effectively.

Fair treatment of *disabled persons* in Cyprus remains ensured. They enjoy privileged access to the public sector as long as their qualifications are the same as those of other applicants. In February 2002, due to an investigation launched by the parliamentary Human Rights Committee, public attention was drawn to the fact that mentally handicapped suspects were not subject to any special treatment. It was agreed between deputies and police representatives that pre-trial detention in prison should be avoided for people with special needs.

Approximately 70% of workers belong to independent *trade unions*, exercising their right under the Constitution. They also enjoy the right to strike, but there were no strikes in 2001.

Cyprus continues to be a party to the *European Social Charter* (both the original and the revised Charter) and the Additional Protocol. Between July 2001 and June 2002, the European Committee of Social Rights examined the 20th report submitted by Cyprus in August 2001. It repeated its previous view that most of the provisions of the Charter are respected, but that Article 1(2) on the prohibition of forced labour was not fully complied with, referring to the still existing Defence Regulations 79A and 79B. These entitle the Council of Ministers to requisition workers in a certain number of cases and to adopt decrees prohibiting strikes. It should be noted that in practice no cases of forced labour occurred during the period under review. According to the European Committee of Social Rights, however, the non-application of these provisions is not sufficient to demonstrate that a state is in conformity with the Charter. In addition, the Committee concluded that the additional duration of sixteen months of alternative service (42 months altogether) as compared with 26 months of military service is excessive and amounts to a disproportionate restriction on the right of the worker to earn his living in an occupation freely entered upon as provided by Article 1(2) of the Charter.

Minority rights and the protection of minorities

Cyprus has ratified the Framework Convention for the Protection of National Minorities. According to Article 2 of the Constitution, all Cypriots are deemed to belong to either the

Greek Community or the Turkish Community. The three minority religious groups – Armenians (0.4%), Maronites (0.6%) and Latins [Roman Catholics] (0.1%) – which were given the option of becoming members of either the Greek or the Turkish Community, opted to belong to the Greek Community. In April 2001, the Advisory Committee on the Framework Convention expressed the view that this constitutional provision is not compatible with Article 3 of the Framework Convention, under which every person belonging to a national minority shall have the right freely to choose whether to be treated as such.. The Council of Europe's Committee of Ministers concluded in February 2002⁹ that this issue needs to be addressed.

In addition to their normal voting rights, the Armenian, Maronite and Latin [Roman Catholic] groups elect non-voting representatives to the House of Representatives who attend as observers and advise on religious and educational matters affecting their group. In its conclusion the Committee of Ministers of the Council of Europe recommended that consideration should be given to making this participation more effective.

In the period under review, the five major religious groups continued to receive government subsidies and to be exempted from taxes. Free education is safeguarded, which is documented by the fact that Armenians run primary schools of their own with financial assistance from the State. The Committee of Ministers took note of these commendable efforts, as well as of the free access to radio broadcasting for minorities.

As observed in the previous Regular Report, Cyprus set up an elementary school for Maronites in 2001. However, given that the 4,500 members of this community are divided between the north and the Government controlled areas following the events of 1974, the survival of the Maronites as a distinct group is still at risk. The Committee of Ministers recommended further measures to promote the conditions necessary for the Maronites to maintain and develop the essential elements of their identity relating to their specific ethnic origin and – at least for some of them – to a specific Arabic dialect.

1.3. General evaluation¹⁰

The Commission has repeatedly concluded that Cyprus fulfils the political criteria. This was the conclusion of previous Regular Reports, and has been confirmed over the past year. Cyprus continues to fulfil the Copenhagen political criteria.

The state public administration has been considerably strengthened by the creation of new posts and the promotion of regular training.

Cyprus continues to respect human rights and freedoms. Cyprus has improved the procedure for the protection of refugees. It has abolished restrictions on the right to marry for Turkish Cypriots living in the south.

⁹ Resolution Res CMN (2002)3 of 21 February 2002.

¹⁰ See "Towards the Enlarged Union: Strategy Paper and Report of the European Commission on the progress towards accession by each of the candidate countries ", COM (2002) 700.

2. Prospects for a political settlement

The UN process

As reported last year, the UN proximity talks were not continued in 2001, and the invitation of the UN Secretary-General to resume the search for a comprehensive settlement in early September had been declined by the Turkish Cypriot side.

After an exchange of letters in late autumn, the leaders of the two communities, Messrs Clerides and Denktash, met on 4 December 2001 and agreed on a different procedure. They stated that “the UN Secretary General, in the exercise of his mission of good offices, would invite them to direct talks, that these talks will be held in Cyprus, starting in January 2002 on United Nations premises, that there will be no preconditions, that all issues will be on the table, that they will continue to negotiate in good faith until a comprehensive settlement is achieved, and that nothing will be agreed until everything is agreed”.

Both leaders crossed the green line for the first time since 1974 and met on 5 and 29 December. They discussed, *inter alia*, how to accelerate the exchange of information on missing persons. At the end of January 2002, papers were exchanged to enable the UN Committee on Missing Persons to resume its activities.

The direct talks started on 16 January 2002 at premises in the United Nations Protected Area in the presence of the UN Secretary General’s Special Adviser on Cyprus, Mr. A. de Soto. The leaders exchanged position papers on the core issues of constitution, security, territory and property. Initially, at the proposal of Mr. Denktash, they envisaged the end of June as a date at which a framework settlement should be ready for signature.

In early May, following an interim report from Mr. de Soto, the members of the UN Security Council issued a press statement. They “expressed the view that it was time to record on paper the areas of common ground between the two sides, with the aim of establishing the component parts of a comprehensive settlement which takes full consideration of relevant UN resolutions and treaties; and, where differences remain, to narrow and remove those through a process of negotiation focussed on compromise formulations. They urged both sides, in particular the Turkish side, to cooperate fully with the Secretary General’s Special Adviser in such an effort”.

With the endorsement of the Security Council, UN Secretary-General Annan visited Cyprus on 14-16 May. He said that, despite their differences on substance and on the timeframe, he was still convinced that between May and the end of June the two sides could resolve all the core issues, provided they acted decisively and with the necessary political will. He also called on Greece and Turkey for sustained and constructive support. Although no joint declaration was issued, the two leaders assured the UN Secretary-General that they would intensify their efforts and continue the talks in a genuine spirit of give-and-take. However, by 2 August, after five rounds of talks, a total of over 50 sessions had been held without agreement on any core issue.

Meeting on 9 July, the members of the UN Security Council heard a further briefing from Mr. de Soto. In a statement to the press, the members “welcomed the support given to the

talks by the EU Heads of State and Government meeting in Seville on 21-22 June” (*see below*). They “expressed disappointment that, despite the Secretary-General’s valuable personal involvement, including when he visited the Island in May, progress remained disappointingly slow and the June target date for agreement had not been met. They noted in this regard that the Turkish Cypriot side had been less constructive in its approach so far and had declined to support the goal of resolving the core issues by the end of June. They also noted with regret that the call by the members of the Council on 2 May that the UN should play a fuller part in the talks had not yet received the requisite response”. The members “urged both sides to work with the UN Secretary-General’s Special Adviser so as to enable him to establish the component parts of a comprehensive settlement which takes full consideration of relevant Security Council resolutions and treaties. They strongly underscored the need for the Turkish side in particular to move in this direction”.

The talks were resumed on 27 August. On 6 September 2002, UN Secretary-General Annan met the leaders of the two communities in Paris. According to his statement to the press, he asked the leaders to go back to the island and to work with Mr. de Soto on the issues that he highlighted to them, and to meet him once more in New York on 3 and 4 October. Mr. de Soto would be working with them to help them to achieve the requisite progress. The Secretary-General said that he continued to believe that the gaps dividing the parties could be bridged and, on some issues, that they were quite a bit smaller than when the talks began.

The UN Peacekeeping Force in Cyprus (UNFICYP) destroyed in April 2002 some 4,500 weapons that had been purchased by the Government of Cyprus in 1972 and later guarded by UNFICYP in the United Nations Protected Area.

The military situation along the cease-fire lines remained calm, and air violations decreased by 50 % during the last year. However, according to the UN Secretary-General’s report of June 2002, restrictions imposed on UNFICYP by the Turkish forces/Turkish Cypriot security forces in July 2000 continued to hamper UNFICYP operations while, similarly, the military *status quo* in the village of Strovilia was unchanged. On June 13, the Security Council extended the mandate of UNFICYP for a further six months to December 2002.

EU position

The conclusions of the European Council at Helsinki in December 1999 remain the basis of the EU position: “...*a political settlement will facilitate the accession of Cyprus to the European Union. If no settlement has been reached by the completion of the accession negotiations, the Council’s decision on accession will be taken without the above being a precondition. In this the Council will take account of all relevant factors.*”

The European Council at Laeken in December 2001 welcomed the meetings that had taken place towards the end of that year between the leaders of the Greek and Turkish Cypriot communities and encouraged them to continue their discussions with a view to an overall solution.

The Seville Summit in June 2002 stated that the EU’s preference continued to be for the accession of a reunited island. It fully supported the efforts of the UN Secretary-General and called upon the leaders of the two communities to intensify and expedite their talks in order to seize the unique window of opportunity for a comprehensive settlement,

consistent with the relevant UN Security Council resolutions, before the completion of the accession negotiations. The conclusions also indicated that the EU would accommodate the terms of a comprehensive settlement in the Treaty of Accession in line with the principles on which the European Union is founded; as a Member State, Cyprus would need to speak with a single voice and ensure proper application of EU law. The EU would make a substantial financial contribution to support the development of the northern part of a reunited island.

The EU has recalled its position to the interested parties on numerous occasions over the last year. Representatives of successive EU presidencies, the European Parliament and the Commission have undertaken visits to the island to explain the EU position.

On 25 October 2001, in a speech held in Nicosia, Commission President Prodi said that reaching a political settlement before the end of the accession negotiations would allow Turkish Cypriots to participate in these negotiations. It would further enable the accession arrangements to take account of the settlement, thus reflecting the concerns of all parties. Commissioner Verheugen visited Cyprus in March 2002 and conveyed to the leaders of the two communities the importance attached by the EU to the achievement of a settlement in good time. He also referred to the Commission's proposal of 30 January 2002 to reserve an amount of € 206 million that could be spent in the years 2004-2006, in the event of a settlement, to help the northern part of the island to catch up.

The prospects for a settlement were discussed at meetings of the EU/Cyprus Joint Parliamentary Committee (in November 2001 and May 2002). The President of the European Parliament, Pat Cox, met the two leaders in Cyprus in early May 2002, and the European Parliament has frequently addressed various issues arising from the political situation.

Commissioner Verheugen has consulted regularly with Mr de Soto, and has been in constant touch with all those in the international community who are active on this issue. Senior Commission officials have held frequent meetings with Greek and Turkish Cypriot leaders and with Mr de Soto's team, notably to clarify *acquis*-related issues arising in their efforts to achieve a settlement. The requirements of the *acquis* in terms of the capacity of a Member State to speak with one voice and to carry out its obligations under the EU Treaties were explained in detail.

The efforts to find a settlement have also been raised regularly in the enhanced political dialogue and in the Association Council with Turkey in April 2002. The EU considers that Turkey has an important contribution to make towards these efforts. The Cyprus problem has also been discussed in bilateral contacts with other third countries, especially permanent members of the UN Security Council.

As requested by the General Affairs Council in 1995, the Commission has continued to promote bi-communal projects, mainly in cooperation with the UN. A EU project manager for civil society projects has begun work in Nicosia, and a first set of projects have been selected by a bi-communal board. Commissioner Verheugen opened an EU information centre within the premises of the Turkish Cypriot Chamber of Commerce during his visit to the island in March 2002. The functioning of the information centre has encountered difficulties. As part of the Commission's information efforts, several lectures on Community policies were given to Turkish Cypriot businesspeople and other

interested persons in the framework of the Chamber of Commerce. These were interrupted in late May due to newly imposed entry restrictions for Commission officials.

Efforts to resolve the Cyprus problem are continuing in the knowledge that the Commission has proposed a financial package to help overcome economic disparities between different parts of the island, following a settlement. This, together with the clarifications provided concerning the *acquis*, has improved awareness throughout Cyprus of the fact that the EU, its *acquis*, institutions and policies favour the efforts of those who are working towards a settlement.

The situation in the northern part of the island

The main political event in the northern part of the island was the holding of local elections on 30 June. The National Unity Party (NUP) won 16 out of 28 municipalities, Republican Turkish Party (RTP) 5, Democratic Party (DP) 4, Nationalist Justice Party (NJP) 2, and one municipality was won by an independent candidate. The Republican Turkish Party which favours a settlement in the framework of a bi-zonal and bi-communal federation and EU accession of a united Cyprus made important advances compared with previous elections and holds the mayor's post in three of the largest cities, including Nicosia.

The opposition newspaper "Avrupa" had its material confiscated in December 2001 following a judicial decision that found the paper's chief-editor guilty of libel against Mr. Denktash. Later on, the paper was re-founded under the name "Africa". A teacher was suspended from her job in November 2001 after writing an article for "Avrupa/Africa" in which she named Turkey as an occupation force in northern Cyprus. On 8 August 2002, the newspaper's editor and an editorial writer were sentenced to six months in prison for an article published in July 1999 that was said to have contained an "insult against the President". The judgement was criticised by the leaders of the Turkish Cypriot opposition parties and several international human rights organisations as a severe violation of the right to free speech. On appeal the judgement was reversed, and the two journalists were released in early October.

Disciplinary measures were taken against those teachers who attended a concert of the Cyprus bi-communal choir in Istanbul in June 2002. They have been accused of "leaving the country without permission of the relevant Ministry in order to perform illegal political activities". In some cases, Turkish Cypriot participants have been denied access to the Ledra Palace or passage to the south for bi-communal events.

The 41 NGOs Platform campaigning under the slogan 'This Country is Ours' called international attention to the deteriorating economic situation, the hardening of repressive policies and has asked for direct involvement of the EU in the search for a political solution. On 9 August, 86 NGOs which represent about 38,000 members, signed a declaration, entitled the "Common Vision of the Turkish Cypriot Civil Society", calling for a solution to the Cyprus problem and EU membership before the end of the year 2002. It states, *inter alia*, that the two politically equal sides should establish a Partnerships state with a single international legal identity and with an effective legislative, administrative and judicial structure that is sufficient to carry out its relationship with the European Union. According to the "Vision", the parties will not be asking for two separate and sovereign states.

On 24 June and 22 July 2002, the Council of Ministers of the Council of Europe agreed to resume consideration of the non-execution of the judgments of the European Court of Human Rights in the cases of *Loizidou* and *Cyprus v. Turkey* at its meeting in October. 110 applications against Turkey concerning the north of Cyprus are pending before the Court.

The *economic situation* in the northern parts of Cyprus is still very weak and the population is undergoing severe hardships more than a year after the economic and banking crises in Turkey had damaged economic activity in the north. Real output growth contracted by 3.6% in 2001, following a 0.6% fall in 2000. Consequently, per capita income has continued to decline in 2001, with the economic crisis aggravating the income gap with the rest of the island. Estimates put income at some €4,000 per head in 2001¹¹.

The northern part of the island has no independent monetary policy and uses the Turkish lira as its currency. As a result, high inflation is imported from Turkey and currently stands at more than 75% on an annual basis. Coupled with an attempted freeze on wages in the large public sector – public-sector wages were raised by only 8% for 2001 – the high inflation rate has undermined real wages. The loss of purchasing power by private-sector workers is of a similar order of magnitude.

The northern part of Cyprus remains heavily dependent on fiscal transfers from Turkey. On an annual equivalent basis, Turkey provides at least € 100-200 million in economic and financial support, in the form of direct aid, loans, subsidies and other grants. Turkey has promised aid of about € 225 million for 2002-2005. However, the amount is set in Turkish lira, which effectively reduces real annual economic support by the high rate of inflation. In addition, in March 2002 it was announced that \$ 260 million will be given according to an investment incentive plan, but here the same remark applies. There have been further agreements on an *ad hoc* basis to support different items such as a protocol signed in July 2002 to finance the purchase of wheat and barley from producers in the north.

High inflation in combination with large trade and budget deficits of around 34% of GDP and 11% of GDP, respectively, have created an economic situation only sustained by transfers from Turkey. Trade is heavily dependent on the Turkish market. A new economic programme, the “Economic Stability and Transition Programme based on Production Growth” was presented in September 2001 and revised in February 2002. Its primary aim is to set up a common economic area with Turkey, thereby further reinforcing the economic dependence on the latter. “Duties” between Turkey and the northern part of the island have been suppressed, as long as products from the northern part of the island have received a certificate of origin issued by Turkish representatives in Nicosia.

The northern part of the island continues to face severe shortages of capital, skills and business. There is an increasing tendency that members of the younger generation with

¹¹ This does not include a large black economy that is currently estimated at 30-40% of GDP. A sizeable black market usually indicates a lack of proper economic market incentives and often partly replaces ‘official’ economic activity, especially during economic breakdowns. As a black economy, by definition, is outside of proper market systems, it is also often very costly in terms of proper economic development.

higher education emigrate to work abroad. The public sector is the largest employer, and public ownership or control is widespread, with price control pervasive. During the first 11 months of 2001, 424 enterprises in the northern parts of Cyprus have closed down, with the textile industry among the most affected. Eight banks have collapsed since late 1999 and the banking sector remains weak.

As last year, output in the agricultural sector, the largest sector in terms of employment after public services, has also increased this year. Rainfall has been sufficient, following severe droughts in recent years. However, the increase in the local supply of agricultural products has led to a decline in prices set by the authorities, although on the other hand credit and fertiliser are still subsidised. Plans to end intervention in agricultural markets in line with the economic and social package have been abandoned.

Educational establishments have become an important source of earnings, generating around 15% of gross income in the northern part of the island. The substantial tourism potential remains largely undeveloped: the northern part of the island possesses some of the most beautiful coastline of the island but only received 84,000 tourists, or 3% of the 2.7 million arrivals in the south.

A political settlement and EU accession

The analysis set out in last year's Regular Report for Cyprus as concerns the prospects for a re-united Cyprus within the European Union remains valid. EU membership, following a political settlement, will provide an effective framework for guaranteeing fundamental democratic and human rights and for raising living standards and reducing disparities in income. Participation in EU programmes and networks and specific EU policies to promote structural adjustment will underpin economic development in the north.

Last year the Commission expressed the view that matters arising from a settlement, which have implications for the *acquis*, could be accommodated in the accession framework in line with the principles on which the European Union is founded. It also pointed out that a Member State was free to determine its own constitutional arrangements provided that it could speak with one voice in the EU decision-making process and ensure fulfillment of its EU obligations. These positions were subsequently set out by the European Council in Seville in June 2002 (*see above*).

The Commission wrote last year that "There is a window of opportunity for reaching a settlement, reflecting the concerns of the respective parties, before the end of the accession negotiations. This will allow the Turkish Cypriots to be part of the accession process and to enjoy the benefits of accession." Progress towards a settlement has been slow and the deadline of end-June for resolving the core issues, set by the Greek Cypriot and Turkish Cypriot leaders themselves, was not met.

All the parties concerned should now make a determined effort to achieve a settlement this year, so that the benefits of accession to the EU of a re-united Cyprus can accrue to all Cypriots.

3. Economic criteria

3.1. Introduction

In its 1993 Opinion on the application of the Republic of Cyprus for EU membership, the Commission concluded:

“The economy of the southern part of the island has demonstrated an ability to adapt and seems ready to face integration provided that the work already started on reforms and on opening up to the outside world is maintained, notably in the context of the customs union.”

In its 2001 Regular Report, the Commission found that:

“Cyprus is a functioning market economy. It should be able to cope with competitive pressure and market forces within the Union.”

In examining economic developments in Cyprus since the first Regular Report, the Commission’s approach was guided by the June 1993 conclusions of the Copenhagen European Council, which stated that membership of the Union requires;

- the existence of a functioning market economy; and
- the capacity to cope with competitive pressure and market forces within the Union.

In the analysis below, the Commission has followed the methodology applied in the previous annual Regular Reports. The analysis in this year’s Regular Report takes stock of developments since 1997.

3.2. Summary of economic developments since 1997

Cyprus has achieved robust economic growth, while the fiscal imbalance has gradually been reduced and the current account deficit has remained rather high. Steady and high real GDP growth averaging 4.2% has been driven mainly by domestic demand, while the high growth in tourism has also contributed significantly. In 2001, real GDP growth was affected by the slowdown of foreign demand, exacerbated after 11 September by a stark decline in tourist arrivals. The government deficit¹², climbed to 5.2% of GDP in 1997, but was steadily brought down to 3.0% by 2001. Despite fiscal consolidation, the current account deficit fluctuated around a relatively high average of 4.5% of GDP with no clear downward trend, heavily influenced by energy prices and defence outlays. Inflation was generally kept under control at an average of 2.7%, dropping to 2% in 2001 after a mainly oil-price and VAT-induced spike to 4.9% in 2000. To confront the challenges posed by greater capital mobility, the Central Bank introduced a more flexible exchange rate regime in 2001.

¹² Harmonised EU standards (ESA95) for 1998-2001; for 1997 national data are used.

Main Economic Trends								
Cyprus		1997	1998	1999	2000	2001	Average	2002 latest
Real GDP growth rate	per cent	2.4	5.0	4.6	5.1	4.0	4.2	2.9p Q1
Inflation rate ^a	per cent	3.3	2.3	1.1	4.9	2.0	2.7	2.3 July
- annual average								
- December-on-December	per cent	3.8	0.8	3.6	3.7	2.1	2.8	3.8 July
Unemployment rate	per cent	3.4	3.4	5.9	4.9	4.0	4.3	:
^d - LFS definition								
General government budget balance	per cent of GDP	:	:	:	:	:	:	
Current account balance	per cent of GDP	-4.0	-6.7	-2.3	-5.2	-4.5	-4.5	
	million ECU/€	-299	-541	-204	-495	-457p ^e	-399p	:
Gross foreign debt of the whole economy	per cent of exports of goods and services	312.4	138.2	164.5	162.4	:	:	
- debt export ratio								
	Million ECU/€	11,030	4,892 ^b	6,350	7,121	:	:	
Foreign direct investment inflow	per cent of GDP	0.9	0.8	1.3	1.8	1.8	1.3	
- balance of payments data								
	million ECU/€ ^o	67	62	114	174	182 ^e	120	:

Sources: Eurostat. National sources. OECD external Debt Statistics

^a PROXY HICP since 1998 (see methodological notes).

^b series break as a result of some technical changes to the definition. Data adjusted from 1998 for offshore centre financial activity.

^c Moving 12 months average rate of change.

^d 1997 and 1998: Registered unemployment. As from 1999: Largely EU-harmonised LFS.

^e Source: Website of the National Bank.

The restructuring and liberalisation process to align with the acquis has been moving forward in various areas, most notably the financial sector. Against the background of Cyprus' application for EU membership there was a need to address a number of rigidities in the economy and to increase flexibility. Recently, good progress has been achieved in trade and price liberalisation and privatisation. Cyprus has also worked toward an extensive adjustment of the financial system. Over the period, further

deregulation and easing of foreign exchange and capital controls have proceeded gradually, thus allowing time for adjustments. A major step forward was the unproblematic abolition in January 2001 of the long-standing interest rate ceiling¹³. Capital account liberalisation has not led to any major problems and has been accompanied by increased inward and outward flows, while the exchange rate has remained relatively stable throughout. Progress in health sector reform stalled somewhat in 2001 after Cyprus had embarked upon an ambitious healthcare reform agenda in 2000 to address fragmented provision of services, congested healthcare provision and rising costs. Water is a crucial scarce asset on the island and poses pressing environmental challenges, but the supply side situation has been improving somewhat through the construction of desalination plants and more normal rainfall this year.

Starting from relatively high income levels, catching up towards the EU average has made good progress. In 2001, GDP per capita in purchasing power standard (PPS) as a percentage of the EU average reached 80%. The situation in the labour market has been favourable and close to full employment throughout. The employment rate is relatively high at 67.9% in 2001, up from 64.2% in 1999. The male employment rate is particularly high, at 79.7% in 2001. The overall unemployment rate remained very low and stood at 4% in 2001, averaging only 4.3% over the period. The unemployment rate for young people (under 25) fell from 11.9% in 1999 to 8.4% in 2001. The gap between male and female unemployment remained relatively wide, with on average 3.6% for males and 6% for females. Long-term unemployment remains limited and stood at 21.9% of all unemployed in 2001. There is a comprehensive social security system, buttressed by a powerful informal social safety net based upon the family.

Main Indicators of Economic Structure in 2001		
Population (average)	Thousand	762,3
GDP per head ^a	PPS	18,500
	per cent of EU average	80
Share of agriculture ^b in:		
- gross value added	per cent	3.9
- employment	per cent	4.9
Gross fixed capital formation/GDP	per cent	:
Gross foreign debt of the whole economy/GDP ^c	per cent	74.9
Exports of goods & services/GDP	per cent	46.9
Stock of foreign direct investment	Million €	:
	€ per head ^a	:
Long term unemployment rate	per cent of labour force	0.9

¹³ This ceiling had been in place since the early 1940s, when it was introduced by the British administration of the island to combat extortion.

- ^a Figures have been calculated using the population figures from National Accounts, which may differ from those used in demographic statistics.
- ^b Agriculture, hunting, forestry and fishing.
- ^c Data refer to 2000.

3.3. Assessment in terms of the Copenhagen criteria

The existence of a functioning market economy

The existence of a functioning market economy requires that prices, as well as trade, are liberalised and that an enforceable legal system, including property rights, is in place. Macroeconomic stability and consensus about economic policy enhance the performance of a market economy. A well-developed financial sector and the absence of any significant barriers to market entry and exit improve the efficiency of the economy.

There has been broad consensus about the key objectives of economic policy. Accession to the European Union enjoys wide support among all political parties. In August 2002 the Cypriot authorities presented their second Pre-accession Economic Programme (PEP) to the European Commission. As last year, the programme was adopted by the Council of Ministers, presented to Parliament and (in a slightly modified version) made publicly available. The PEP is taking an increasingly strategic role in economic policy and is now a reference point for the authorities. Its preparation helped to increase co-ordination between the key economic policy-making institutions - the Ministry of Finance, the State Planning Bureau, and the Central Bank - in creating a consistent medium-term policy framework.

Cyprus has maintained robust economic growth. Between 1997 and 2001, the economy grew by an average 4.2% annually. Domestic demand has been a primary growth motor, with consumption fluctuating around a period average of 5.8% while investment varied from high positive to negative growth rates resulting in a period average of 1.5%. Fluctuations in consumption were primarily linked to expected and actual VAT and excise taxation changes and, to some extent, local stock market developments. Public sector investment was more volatile than private sector investment. A rapid increase of services exports, in particular in the tourism sector, has been another primary source of growth. Import growth at 3.7% was on average marginally higher than export expansion at 3.5%, while both growth rates fluctuated significantly over the period. After reaching 9.1% growth in 2000, total real exports of goods and services are estimated to have increased by 4.1% in 2001. The slowdown in import expansion to 4% in 2001, linked to stagnation in tourism and investment, plus a slight terms of trade improvement, led to a slight reduction in the current account and trade deficits in 2001. In 2001 the economy slowed down to a still respectable 4.0% growth, from 5.1% in 2000. Following the stark decline in tourist arrivals after 11 September, the overall tourism growth rate was flat in 2001. Initially, domestic demand was also affected as business and consumer confidence deteriorated, but investment and consumption growth for 2001 held up relatively well at 5% and 1.4%, respectively. For consumption this has been the more remarkable, given the negative wealth effect after the bursting of the stock exchange bubble in 2000. First estimates for the first quarter of 2002 show a year-on-year GDP growth of 2.9%, the lowest quarterly growth since 1997.

Over the period 1997-2001, the tourism sector continued to grow very rapidly, but slowed down after 11 September. Tourist arrivals in the period 1997-2001 increased on average by 6.7% annually, benefiting *inter alia* from a nominal appreciation of the British pound vis-à-vis the Cyprus pound. However, after 11 September arrivals fell dramatically, resulting in nearly flat growth for the full year, although tourism revenue still grew by 7%. The period January-June 2002 saw a continuation of this downward

trend with arrivals down by 12.6% compared to the same period of the previous year. For 2001 this still adds up to 2.7 million tourists visiting the southern part of the island and tourism receipts representing 22% of GDP, up from 19% in 1997.

Despite fiscal consolidation and increased tourism receipts, the current account deficit remains fairly high. The high 1997-2001 trade deficit of on average 27.3% of GDP has been largely offset by a surplus on the invisibles balance of 23% of GDP, mainly thanks to tourism, offshore business and other services, resulting in a current account deficit fluctuating around 4.5% of GDP. Although tourism has grown vigorously and the fiscal deficit has steadily been brought down, there has been no clear improvement in the current account deficit over time, suggesting that private sector savings as a share of GDP have declined. Inward foreign direct investment (FDI) was on average 1.3% of GDP, increasing from 0.9% in 1997 to 1.8% in 2001 as capital liberalisation progressed. Total outward investment more or less balances out inward investments (FDI and portfolio investment), so that coverage of the current account deficit by net foreign investment is limited. As a result, total external debt has been gradually increasing, from 60.2% of GDP in 1998 to 74.9% by end-2000¹⁴. External debt of the financial private sector was negligible at 4% of total debt in 2000. However, capital liberalisation did lead to increased private sector borrowing abroad in 2001, rapidly increasing its share of total external debt to just under 25% in 2001. Although this was most likely the result of a portfolio adjustment following capital liberalisation, further developments need to be monitored. Financing the current account deficits has not been problematic so far and the level of international reserves at present amounts to 25 months of imports. Nevertheless, the current account deficits do systematically put upward pressure on debt levels and could become a cause of concern.

The labour market has been operating close to full employment. The average registered unemployment rate for the period 1997-2000 was 4.3%. In 1999 it stood at 5.9%¹⁵, rapidly dropping to 4% by 2001. Although the market seems rather tight at first sight, labour market shortages and wage pressures are partly deflected by seasonal immigrant workers. The foreign labour share in total employment has steadily increased over time and stood at 10% of the gainfully employed labour force in 2001. The wage-setting system, based on central bargaining, has also helped to prevent inflationary overheating.

The average inflation rate has been kept low, and fell in 2001. The average inflation rate based on the EU harmonised index of consumer prices (HICP) for 1997-2001 stood at 2.7%. The peg to the ECU and then the euro, trade liberalisation, increased competition in domestic markets, fiscal consolidation, and relatively low wage pressures were among the main factors keeping inflation down. Due to a number of one-off factors, including high oil prices, drought and increases in VAT rates, inflation jumped to 4.9% in 2000. Afterwards, it fell back to 2% when the transitory effects had subsided. The year-on-year inflation rate in July 2002 stood at a relatively high 3.8%, which was mostly due to increases in excise duties and VAT.

¹⁴ The ratio given here does not include international banking institutions. Such institutions hold large volumes of both foreign assets and liabilities with zero net positions and their transactions have only limited impact on the local economy. Including these for 2000 would give a gross debt ratio of 162%.

¹⁵ The unemployment rate was based on registered unemployment until 1998; since 1999 onward labour force survey (LFS) methodology has been used.

Monetary policy has managed to control inflation. Monetary policy has been consistently geared to maintaining price stability. The Central Bank of Cyprus (CBC) has gradually moved away from the use of direct instruments for controlling liquidity toward market-based tools. The independence of the CBC was formally established in line with EU requirements in 2002¹⁶ and price stability is now its formal prime objective. Concurrently, the reliance on the CBC for financing the government deficit – unusual among developed countries – has ended. Although in the past such financing was considered a last resort, the facility was used rather often, particularly in 2000, when the whole of the government deficit was thus financed, and up to its abolition on 1 July 2002.

Liberalisation of the financial markets has progressed, posing new challenges for monetary and exchange rate policies. A number of further important changes in monetary and exchange rate policy were introduced to adjust to the liberalisation of – notably outward – capital flows. To increase flexibility of the exchange rate regime in response to the increasing challenge of greater capital mobility, the CBC widened the fluctuation margins of +/-2.25% around the central parity vis-à-vis the euro to +/-15%. Although these measures could have been accompanied by higher volatility in interest and exchange rates, this has not materialised and the Cyprus pound essentially remained stable while reserves increased. On 1 January 2001, the authorities also scrapped the long-standing interest rate ceiling and simultaneously liberalised medium- and long-term borrowing in foreign currency. Additional charges, endemic under the old regime and essentially substituting for higher interest rates, have now disappeared. Banks are now free to apply the spreads on their lending according to their assessment of risk and the credit rating of the client. After the further liberalisation of the capital account, resident foreign currency borrowing (mostly in euro) increased sharply in 2001, leading to increased liquidity growth. Given low inflation, to counter lower growth prospects after the summer the CBC decided in August 2001 on a pre-emptive move to reduce interest rates. Altogether, interest rates were lowered three times in the course of 2001 to reach a historically low 5.5% by the end of the year. As a result of the concomitant reduction of the differential between domestic and foreign interest rates, private sector foreign borrowing fell sharply in 2002.

The general government fiscal deficit has declined notably since 1997. Following the slowdown in economic activity in 1996, the general government deficit expanded to unsustainable levels in 1997 and 1998, reaching 5% of GDP, as government spending increased rapidly. In response to the deteriorating fiscal position, in 1999 the authorities introduced the Strategic Fiscal Consolidation Plan (SFCP). The programme, revised and extended in 2001 and again in 2002, aimed at reducing the deficit to 2.0% of GDP by 2002 and is to reach fiscal balance by 2005 (previously 2004). This is to be achieved through expenditure restraint, notably through lower public sector employment expansion after rapid growth in 1997-1999 and, for 2002, a cut in defence outlays after high growth in 2001. The SFCP has been successful so far, although slippage occurred in 2001. The general government deficit fell sharply, particularly after July 2000 when VAT rates were increased a first time. The general government consolidated deficit was brought down from 5.2% of GDP in 1997 to 3.0% in 2001, while the primary surplus (the government budget balance corrected for interest payments) increased from 0.5% of GDP to 2.7% of GDP. The overrun in 2001 occurred despite a substantial increase in tax revenues and

¹⁶ In July 2002, Parliament approved the fourth amendment to the Constitution and the relevant bill establishing the independence of the Central Bank of Cyprus

was caused by somewhat slower economic growth and increases in defence expenditure. The budget for 2002 was recently approved and sets a deficit target of 2.6%, which is above the original target commitment.. In the period 1998-2001, general government gross debt as a percentage of GDP held more or less steady at an average of 55.5% of GDP, declining to 54.6% of GDP in 2001.¹⁷ The fiscal consolidation programme aims to bring the debt-GDP ratio on a downward path.

Major tax reforms have recently been introduced. In addition to the SCFP, a major tax reform was approved by Parliament in July 2002. The reform marks a considerable shift from direct to indirect taxation. The reform includes, *inter alia*, further increases in excise and VAT rates to EU levels, higher social security contributions to improve sustainability of the pension system, a lowered uniform (for both local and offshore business) corporate tax rate of only 10%, lower personal income taxes, and a gradual abolition of the defence levy. Although the reform is presented as budgetary neutral it could well raise revenues, especially through further harmonisation of VAT rates and excise taxes.

Fiscal policy was tightened while monetary policy has managed to keep inflation low under increasingly challenging conditions. In the period 1997-2001, average national savings were kept low at 15.4% of GDP by high government deficits, while average investment was 19.9% of GDP, leading to an average savings-investment gap, or current account deficit, of 4.5%. The savings ratio varied without a clear trend despite fiscal consolidation, suggesting that private sector savings dropped, while the investment ratio tended to diminish somewhat. The fiscal consolidation was welcome to support monetary policy in keeping inflation low, while it was confronted with the capital account and interest rate liberalisation. With the CBC committed to maintaining a relatively fixed exchange rate regime, fiscal policy will have to keep to the fiscal consolidation programme in order to put downward pressure on current account deficits to more sustainable levels, widen the space for the financing of private sector investment, create room for fiscal manoeuvrability when facing external shocks and lessen the challenges for monetary policy.

With the main exception of petrol, the vast majority of prices are freely determined. A process of liberalising administered prices of commodities started in 1997 and by early 2002 few controlled prices remained. In 2001, some of the residual price controls, on common bread and milk, were removed as well. The only controlled prices remaining are for petrochemicals and cement, although in 2000 the Cypriot authorities did partially liberalise petrol prices to replace a price stabilisation scheme capping petrol prices. This scheme proved to be very costly when world oil prices rose sharply. While the new system links the domestic price more closely to world prices, subsidies continue as the system still guarantees a 12% net profit on investment to oil companies and as farmers were exempted from the price increases.

The private sector largely dominates the economy. In 2000, the private sector produced around 75% of GDP, similar to the share in 1997. State monopolies remain in telecommunications, energy, and air transport. In addition, the state owns a majority in five private sector enterprises and has a small equity participation in another two

¹⁷ General government debt data for 1997 are not available. Data for 1998-2001 are as provided by the government. However, the treatment of government sinking funds is not in accordance with EU standards; taking this into account would raise the debt ratio to around 62% of GDP.

enterprises. The value of these shares is equivalent to 0,8% of GDP. The 88% ownership of the Cyprus Development Bank will be reduced to 45% by accession. In 2000 the government reduced its' stake in Cyprus Airways to 69.6% while last year the government privatised the Cyprus Tourist Development agency¹⁸. The authorities are committed to liberalising the telecom, energy, air transport and postal services sectors by 2003. First steps to deregulate the telecom sector have been taken this year with the appointment of a regulator and launch of a call for interest for a strategic partner in the mobile telecom market. Tentative moves to open up air transport routes have also started with limited designation of routes to private enterprises. The process is moving along only slowly in order to give Cyprus Airways a chance to prepare itself for the additional competition.

The business climate is generally favourable. Cyprus' economy has been dominated by SMEs, as only 36 enterprises can be classified as large companies based on the EU definition for SMEs. The environment in Cyprus is conducive to private initiative and SME policy is overall in line with the principles and objectives of EU enterprise policy. Market entry is relatively straightforward in most sectors and bankruptcy procedures operate efficiently. However, although first steps toward liberalisation have been made, barriers to entry in several key sectors remain, with several semi-government organisations benefiting from legal monopolies, including telecommunications and electricity. The liberalisation of the financial markets and planned liberalisation in other sectors together with the tax reform also are conducive to further improvement in the business climate, while the increasing FDI inflows testify to a positive assessment from the market. Cyprus has a relatively small but important offshore sector covering a wide range of activities, including re-exports and financial services. Cyprus is an important regional business centre on the strength of its legal structure based on UK law and practice, tax incentives, an extensive network of double tax treaties, advanced infrastructure, highly educated manpower, and strategic geographic location with extensive links to Middle Eastern and Central and Eastern Europe markets. The preferential tax arrangements enjoyed by the offshore sector¹⁹ also introduced distortions in the allocation of resources in the economy, which the recent tax reform has now eliminated. Given the still low new corporate tax rate of 10% and the other competitive advantages, the government is confident that this will not have a major negative impact on the activities of international business. The services provided are more restricted than in other offshore centres, being confined to a limited number of banks, some insurance services, and some relatively small-scale fund management and advisory business. Banking has been the most important offshore activity (followed by commerce).

Cyprus has a highly effective legal system, with a well-established body of commercial law. Indeed, the relative strength of its legal system was a major contributory factor to the growth of the offshore sector. Property rights are well established in the southern part of the island, notwithstanding certain complex political issues arising from the conflict in 1974 and the subsequent de facto division of the island.

The financial system is highly developed, and it provides an effective intermediation between savers and investors. In the period 1997-2001 the private credit-to-GDP ratio

¹⁸ In effect the government privatised the Hilton, which was the sole asset of the CTD.

¹⁹ The offshore corporate tax rate stood at 4.25%

increased from 100% to 126%²⁰. Following gradual liberalisation, banks have been allowed to lend in foreign currency and such lending more than trebled from 4.6% of total lending in 1996 to around 10% in 2001 and early 2002. This increase in foreign borrowing can be considered part of an adjustment process after capital liberalisation, but does pose an increased exposure risk to banks and clients.

The domestic financial sector is relatively large compared to the size of the economy, and banking, which dominates the financial sector, is well developed. The financial sector contributes around 20% of GDP and 9% of employment. With the exception of two small specialised credit institutions (representing 4% of bank assets), the financial sector is entirely in private ownership with both domestic and foreign-owned banks. Over recent years, the banking sector has not experienced any banking crises or payments system disruptions, and bank restructuring has not been associated with bank failures. Although the stock market collapse from end-2000 onward did raise some concerns on bank asset quality, most of the household financing for stock purchases was based on the use of precautionary savings rather than loans. The sector is relatively concentrated, with the three largest banks accounting for nearly 80% of deposits (or 64% if co-operative credit institutions are included). A major development has been the abolition of the 9% interest rate ceiling, permitting banks to set interest rates as they see fit, thus increasing competition. At the same time, faced with a drop in profits, in early 2002 banks increased the spread they charge over the Lombard rate, affecting mostly SMEs. Co-operative credit and savings societies (CCSS) play a major role in collateralised lending to the household sector. Most of the 360 co-operatives are small but a few are quite large and more sophisticated. Together they account for about one-third of total domestic deposits and lending. The CCSS enjoyed a number of legal advantages – most notably exemptions from both stamp duties and required reserve ratios – which placed them at a competitive advantage relative to the commercial banks. A harmonisation process to bring legislation on CCSS in line with the *acquis* is in progress.

The non-bank financial sector is relatively modest but active, and the domestic securities and equities markets have developed rapidly in recent years. Capitalisation of the small bond market increased from 5.1% of GDP in 1997 to 23.6% by 2001. However, there is hardly any trading on this market. Following tax incentives for newly listed companies and a wave of initial public listings, the Cyprus Stock Exchange (CSE) index shot up in 1999 to over 700 by end-1999 (1996=100). This rise did not reflect fundamentals and subsequently the index plummeted mid-2000 and has continued to decline since, standing at 98 by April 2002. CSE market capitalisation rose from around 25% of GDP in 1997 to 150% at its peak in 2000, falling again to 68% of GDP by end-2001 and reaching 51% in April 2002. Remarkably, this substantial drop appears not to have significantly affected the real economy. Nevertheless, investor confidence in the domestic equities market was shaken.

The financial sector is generally healthy and robust but the banking sector needs to be supervised in a consistent manner. The banking sector is generally highly developed and has been profitable while it has had only relatively low non-performing loans to contend with. Nonetheless, increasing competition and liberalisation do present challenges to the banking sector. The private sector part is well regulated and supervised by the CBC. The

²⁰ If loans granted by the co-operative credit institutions are included, total credit as a percentage of GDP increased from 139% in 1997 to 158% in 2001.

Co-operative Development Department will continue to be the supervisory agency for the co-operative part of the sector. In an effort to improve its administrative capacity, the department received additional resources, including more staff and training facilities. This means that similar financial institutions, i.e. commercial banks and the newly transformed co-operative banks, will be supervised by different agencies. It will be necessary to ensure that the supervision by different agencies of similar financial institutions is sufficiently co-ordinated and carried out in a uniform way. The co-operative central bank will retain its role as the primary liquidity management institution for the co-operative sector, but it will be supervised by the central bank. The capital markets and insurance sector will be supervised by other agencies, which will obtain increased staff posts. The stock market collapse provided an important lesson on the importance of capital market regulation, and Parliament has passed legislation strengthening the Securities and Exchange Commission (SEC) and increasing penalties for non-compliance with stock market regulations. However, there is supervisory competition between the SEC and the Cyprus Stock Exchange.

The offshore financial system has been the subject of intense international scrutiny as a location for money-laundering activities and the current situation appears satisfactory. In recent years, the authorities have made strenuous efforts to counter a negative and damaging reputation for money laundering. Approaching EU accession encouraged a large volume of legislative changes to bring Cyprus in line with the *acquis*. In 1996, a comprehensive anti-money-laundering law was put in place. In 1999, the law was further amended to improve customer identification procedures. The authorities have also developed an information reporting system that has improved the detection of suspicious transactions. The OECD Financial Action Task Force praised the legislative framework now in place, while a 2001 IMF assessment of the offshore financial sector indicated that supervision was generally effective and thorough, although it also noted some scarcity of personnel resources. The supervisory capacity is satisfactory and broadly in line with the *acquis*, with full alignment expected by the end of 2002. Nevertheless, continued protective vigilance is required.

The capacity to cope with competitive pressures and market forces within the union

The ability to fulfil this criterion depends on the existence of a market economy and a stable macroeconomic framework, allowing economic agents to make decisions in a climate of predictability. It also requires a sufficient amount of human and physical capital, including infrastructure. State enterprises need to be restructured and all enterprises need to invest to improve their efficiency. Furthermore, the more access enterprises have to outside finance and the more successful they are at restructuring and innovating, the greater will be their capacity to adapt. Overall, an economy will be better able to take on the obligations of membership the higher the degree of economic integration it achieves with the Union before accession. Both the volume and the range of products traded with EU Member States provide evidence of such integration.

Cyprus has a sufficient degree of macroeconomic stability for economic agents to make decisions in a climate of stability and predictability. It has a solid track record of macroeconomic stability with low inflation and unemployment and improved fiscal control. This creates basic conditions for coping with competitive pressures.

Cyprus has a strong human capital endowment. Over recent years, the tertiary education sector has been strengthened. In 1990, the University of Cyprus was established, and in subsequent years, its activities and facilities have been expanded. Several private sector tertiary institutions have also been established. Since the establishment of the university, the proportion of employed persons who have received tertiary education has risen from just under 20% to over 28%. The government also instituted a reform of higher secondary education during the school year 2001-2002 to meet growing demands for flexibility in the labour market, and announced the establishment of an Open University to create access to university education within the context of lifelong learning.

Labour market policies are aimed at increasing the labour supply and its skill level, while labour market legislation is being aligned with the acquis. The quantitative targets set out in the Strategic Development Plan, covering the period 1999-2003, provide for an annual increase of employment of 1.2% whilst keeping the registered unemployment rate at 3%. The government is committed to mobilise additional domestic labour supply and raise skill levels in the labour force, including a more active role for the public employment service, completion of reforms in education and training, and measures to improve women's access to the labour market. Wage setting is determined under a central system of collective bargaining with a half-yearly automatic backward-looking indexation adjustment to cost of living (COLA). The labour market has been flexible in many respects and labour relations have been peaceful. However, the system still displays rigidities in the face of external shocks, undermining competitiveness and locking in inflationary pressures. The government has opened a dialogue with social partners to discuss reforming the COLA to make it more responsive to market conditions although a shift towards forward-looking indexation or abolition is not on the agenda.

The physical capital stock, including infrastructure, is well developed, but investment has tended to decline in relation to GDP, while R&D is low. A comprehensive system of motorways links all the major cities. The telecommunications system is technologically advanced, while Internet services have grown rapidly. The authorities have launched major projects to upgrade the two international airports at Paphos and Larnaca through a public-private partnership. The gross capital formation ratio in 2001 stood at only 17.3% of GDP, a gradual 2 percentage points decline from 1997. Given the high and sustained growth rate, the efficiency of investment seems to be high. Nevertheless, to sustain high growth rates, a higher investment ratio could be needed. FDI inflows have increased over time as capital liberalisation progressed. Inward FDI reached around 0.9% of GDP in 1997 but then rose notably from 1999 onward to 1.8% in 2001. During the same time, research and development (R&D) expenditures hovered around only ¼% of GDP. Cyprus is taking part in the Fifth Framework Programme, as well as in other Community programmes. Despite progress made in recent years in the promotion of R&D activities, Cyprus' record in this area can still be significantly improved.

Cyprus has challenging water supply and pricing issues. Water is a crucial resource for the economic development of the island. It has suffered from a long-term decline in rainfall levels, while the period 1995-2001 also saw a severe drought. This year's rainfall has been better, with surface water stocks climbing to 60% of capacity against less than 20% last year. However, over recent decades the island's aquifers have deteriorated significantly and aquifer water levels are still at extremely low levels, leading to environmental degradation. As a consequence, the authorities had been forced to ration supplies in particular to the agricultural sector which, under normal conditions, takes about three-quarters of the annual water supply (although it accounts for only about 5%

of GDP). In reaction, farmers resorted to pumping water directly from aquifers. Rationing has stepped down now. In an earlier response two desalination plants were built. A third plant should be operational by April 2004, and a fourth plant is planned. The two plants supply around 40% of domestic household water demand. When the third plant becomes fully operational, desalination capacity will be sufficient to meet 50% of domestic household demand. Water-pricing policy for the agricultural sector needs to be adjusted to more accurately reflect production costs, as water supply prices for this sector are extremely low. Proposals to increase retail prices on the basis of full cost recovery tariffs have been approved by Parliament in 2002.

The contribution of industry and agriculture to GDP and employment has gradually declined throughout the period 1997-2001 with a shift toward services, notably tourism. The share of manufacturing and agriculture in GDP fell from 27% to 24%. The agricultural sector is heavily concentrated in irrigation-dependent products, such as citrus fruits and vegetables, and consumes around three-quarters of the annual water supply. Moreover, the sector enjoys significant water-related subsidies. In manufacturing, the earlier prolonged period of government protection delayed adaptation to competitive conditions while the small size of enterprises, low R&D and level of technology adaptation pose structural problems for manufacturing. In the Five-Year Strategic Development Plan covering the period 1999-2003, the government elaborated schemes for the restructuring of the private sector in specific sectors. Nevertheless, with tourism as a main driving force, the economy is increasingly service-oriented. Although rising tourism dependence is to a certain extent unavoidable for a small open economy with a strong comparative and competitive advantage, such undiversified dependence increases vulnerability.

*Cyprus has a strong entrepreneurial culture, especially in services, demonstrated by the large number of (mainly) small, and medium-sized enterprises. The environment in Cyprus is conducive to private initiative and SME policy is overall in line with the principles and objectives of EC enterprise policy. They are mostly found within the services sector, particularly within the tourism industry, which has grown rapidly over the years. SMEs already benefit from Community initiatives such as the Multiannual Programme for Enterprises and Entrepreneurship. Private sector institutions participate in both the formulation and the monitoring of implementation of sectoral policies and maintain close contacts with their counterparts in the Member States and at EU level. Access to finance for SMEs has been improved with guarantees for loans and interest rate subsidies and a scheme for start-up loans, but there is still room for further progress. A one-stop shop has been set up within the Ministry of Commerce, Industry and Tourism to provide guidance to international enterprises searching for local partners. A specific chapter on SMEs was included in the Five-Year Strategic Development Plan (1999-2003), aiming at, *inter alia*, the creation of a simplified legal and institutional framework for SMEs and increasing SME competitiveness. As regards the implementation of SME policy in Cyprus, sufficient infrastructure has been created in the period 1997-2001.*

The economy has made much progress in moving away from a protected environment towards greater competition. Although the direct share of the government sector in GDP was relatively modest, in the past government policy and legislation provided a sheltered environment for the private sector. Authorities took a protectionist and interventionist approach to industrial policy that favoured domestic producers at the expense of foreign competitors. Before and during the period 1997-2001, steps were taken to liberalise trade, and a number of markets such as the financial market are working towards an

environment more conducive to sustained growth. Nevertheless, identification of trade barriers, implementation of the mutual recognition principle and amendment of legislation remain of concern. Progress with adaptation and implementation of the competition policy chapter and on state aid has been impressive. At the same time the government has adopted the EU industrial policy approach and has now started to open up key sectors of the economy, including air transport, electricity, telecommunications and postal services. However, some ministries have delayed *acquis* implementation and this could hamper the full exploitation of the internal market by companies.

Cyprus is a highly open economy and concentrated on relatively few export products. Trade openness (total exports plus imports as a percentage of GDP) hovered around 98.6% over 1997-2001 and stood at 99% in 2001. Moreover, international trade is well integrated with the EU, accounting for on average 49% of Cypriot exports and 51% of imports. However, these data understate the extent of integration between Cyprus and the EU. The majority of tourist arrivals come from the EU, with around half coming from the United Kingdom alone. Reflecting its central regional location, it also has intense trade relations with the countries of Central and Eastern Europe and the Middle East. Goods imports are mainly consumer and investment goods while goods exports consist mainly of agricultural products and low value added manufacturing goods such as textiles.²¹ The economy has become increasingly dependent on tourist revenues and financial services, while many traditional sources of export earnings, particularly within the manufacturing sector, have suffered a long-term decline. The authorities are keenly aware of the issue and have made efforts to encourage alternative sources of export earnings. However, Cyprus has a powerful comparative advantage in tourism and financial services sectors which has tended to overwhelm government initiatives designed to diversify the economy.

Labour productivity is relatively high and rising. Labour productivity increased from 81% of the EU average in 1997 to 89% in 2001. Most of this clear improvement seems to have been realised in the services sector rather than in manufacturing. At the same time, the Cyprus pound in nominal terms tended to depreciate very slightly against the euro while the real effective exchange rate fluctuated somewhat each year but on average depreciated by only 0.4% annually.

3.4. General evaluation²²

Cyprus is a functioning market economy and it should be able to cope with competitive pressure and market forces within the Union.

The first 1998 Regular Report already acknowledged the economic reform efforts undertaken by the Cypriot authorities to prepare for EU accession. Since then, the Cypriot authorities' commitment to the economic requirements of EU accession has been sustained.

Further improvements can be made to the functioning of markets by keeping to plans to liberalise the telecom, energy, air transport and postal services sectors. Adherence to the

²¹ This refers to domestic exports; half of total goods exports are re-exports, mainly cigarettes and vehicles

²² See "Towards the Enlarged Union: Strategy Paper and Report of the European Commission on the progress towards accession by each of the candidate countries ", COM (2002) 700.

fiscal consolidation programme will contribute to reducing the current account deficit. Care must be taken to improve co-ordination of the supervision of co-operative financial institutions and banks.

4. Ability to assume the obligations of membership

Introduction

This section addresses the question of Cyprus's ability to assume the obligations of membership – that is, the legal and institutional framework, known as the *acquis*, by means of which the Union implements its objectives. Alongside an evaluation of relevant developments since the 2001 Regular Report, this section seeks to provide an overall assessment of Cyprus's ability to assume the obligations of membership, and of what remains to be done. Furthermore, it includes an evaluation of Cyprus's track record since the 1998 Regular Report on Cyprus. It also provides, for each of the negotiating chapters, a summary evaluation of the extent to which commitments made in the negotiations have been implemented, as well as an overview of transitional arrangements that have been granted.

This section is structured in accordance with the list of 29 negotiating chapters, and incorporates an assessment of Cyprus's administrative capacity to implement the *acquis* in its various aspects.

In December 1995, the Madrid European Council remarked on the need to create the conditions for the gradual, harmonious integration of the candidate countries, particularly through the adjustment of their administrative structures. Taking up this theme, in Agenda 2000 the Commission underlined the importance of effectively incorporating Community legislation into national legislation, and the even greater importance of implementing it properly in the field, via the appropriate administrative and judicial structures. This is an essential precondition for creating the mutual trust indispensable for future membership.

In June 2002, the Seville European Council repeated how important it was that candidate countries should continue to make progress with the implementation and effective application of the *acquis*, and added that candidate countries must take all necessary measures to bring their administrative and judicial capacity up to the required level. Building on the assessment of Cyprus's administrative capacity provided in the 2001 Regular Report, the present Report seeks to add further depth and detail, focusing on the main administrative structures required for implementing the various aspects of the *acquis*.

In its 1998 Regular Report on Cyprus, the Commission concluded:

"As regards the adoption of the acquis, a large number of the instruments required for the progressive adaptation of the acquis are already contained in the 1973 association agreement and the 1987 protocol. On the basis of these instruments, Cyprus has made significant progress in adopting the acquis most notably in the context of the customs union. However, substantial efforts have yet to be undertaken in the internal market field and, in particular, in the offshore and financial sectors.

Furthermore, maritime transport, telecommunications as well as justice and home affairs constitute other areas of particular concern. Cyprus should not face major problems in adopting the acquis with regard to the 16 chapters already screened.

As concerns Cyprus's administrative and judicial capacity to apply the acquis, it seems that major problems will not be encountered. However, administrative capacities remain to be strengthened in a number of areas, including the internal market, maritime transport, telecommunications, environment, and justice and home affairs."

In the 2001 Regular Report, the Commission found that:

"During the period covered by this Regular Report, Cyprus has achieved substantive progress in different areas of the acquis and has continued at steady pace with further legislative alignment as well as with the setting up and upgrading of the necessary administrative institutions. The alignment process has gradually accelerated. However, there remain still a considerable number of laws to be adopted.

Over the last year, there has been progress in important areas of the internal market. Concerning free movement of goods, the adoption of EN standards has been accelerated and new legislation was passed as regards sector specific legislation. However, continuing serious efforts are required to transpose and implement the acquis, in particular as regards the framework law on the new and global approach principles and subsequent regulations for the transposition of the New Approach Directives. Furthermore, an overall strategy for better co-ordination of the authorities responsible for market surveillance should be developed. Although Cyprus has undertaken certain measures to abolish inconsistencies with the acquis in the area of free movement of persons in particular as regards the co-ordination of social security systems, important legislative work remains to be done before accession. Concerning financial services good legislative progress can be reported, and the overall standard of supervision appears to be satisfactory. Particular importance should be given to the restructuring of the co-operative and saving societies sector. The liberalisation of capital movements has continued and should be maintained to ensure a proper functioning of the markets upon accession. Significant measures to combat money laundering have been undertaken e.g. with the inclusion of lawyers and accountants within the scope of application of the relevant legislation. Cyprus has also tightened its measures relating to the identification of account holders and reporting of transactions in accordance with the recommendations of various international fora. The harmonisation process should be accelerated with regard to intellectual and industrial property rights. The effective application and enforcement of state aid rules, including the alignment of existing aid schemes as regards in particular the tax regime for the off-shore sector, should be ensured.

Partial progress has been made in the field of agriculture but substantial elements and mechanisms of the acquis remain to be applied as regards in particular the Common Market Organisations and the veterinary and phytosanitary sectors.

In the field of fisheries the reinforcement of the administrative capacity has continued. Additional progress is needed with regard to the current and planned structure of the fishing fleet under Cypriot flag. Significant progress has been made in nearly all sectors of transport policy particularly as regards maritime transport where safety controls have been improved. The performance of the classification societies should be monitored.

While recognising the efforts made and the initiatives taken to further align the tax legislation with the acquis by way of e.g. the scheduled tax reform, concerns remain on

the harmonisation of the level of indirect taxation and the special regime of direct taxation for off-shore companies.

Concerning telecommunications, there is a considerable delay in the adoption of legislation and the preparation of secondary regulatory instruments to transpose key parts of the acquis.

On environment, good progress can be reported. Cyprus has continued with harmonisation measures both as regards legislative alignment as well as strengthening administrative capacity. Particular attention should now be paid to proper implementation and enforcement.

In the area of justice and home affairs progress has been made in particular in the fields of border control, migration and in the fight against corruption and fraud. On asylum, although the administrative capacity has been strengthened with the setting up of a refugee authority, no legislative progress can be reported. In the light of increasing numbers of application alignment should be accelerated as regards in particular the criteria for applications and the setting up of an independent appeal authority.

Cyprus has achieved considerable progress in the field of customs, leaving only some areas where further alignment is necessary, in particular as regards temporary importation, customs procedures with an economic impact and cultural goods.

As regards financial control, Cyprus' financial control system is sound and consistent with European standards; efforts should be undertaken as to the internal control of revenues and the proper management of pre-accession funding and structural funds.

Over the last year, Cyprus has continued sustained efforts to further strengthen its administrative capacity. Training programmes have been organised in different sectors, such as co-ordination of social security systems, maritime safety, and justice and home affairs. Furthermore, additional staff has been recruited in key areas such as financial services, company law, veterinary and phytosanitary issues, fisheries, transport, taxation, social policy and employment, telecommunications, environment and justice and home affairs. This allowed Cyprus to reinforce market surveillance systems in the field of free movement of goods, to improve the due supervision of financial services, to upgrade the inspection arrangements in the veterinary and phytosanitary field and to strengthen its labour inspectorates.

New administrative structures have been set up in order to efficiently apply the acquis. Among these are an authority to settle disputes as foreseen in the credit border transfer Directive, a state aid monitoring authority, a new unit within the Department of Road Transport to deal with market access, a Statistical Council, a special group of officials to examine in detail the new structures of the government with regard to equal treatment of men and women, and finally a refugees authority. In other cases, the powers of the existing enforcement bodies have been increased, such as in the case of the Securities and Stock Exchange Commission, the Unit for Combating Money Laundering (MOKAS) and the Commission for the Protection of Competition. Finally, there are plans to set up a new body on pharmaceuticals (Drugs Price Control Committee). In the field of customs, Cyprus has recently started to introduce an updated version of the IT system so as to allow for the exchange of computerised data with the Community.

In future, it is advisable to reinforce the administrative infrastructure for standardisation and certification to enhance the free movement of goods. Further efforts should also be made to strengthen enforcement capacity in the field of intellectual property rights, especially as regards border controls and fight against piracy and counterfeiting. Although progress has been made both in the fields of anti-trust and state aid, the infrastructure, staff, and the rather weak enforcement record of the anti-trust legislation should be improved. As regards taxation, Cyprus should develop IT systems, so as to allow exchange of electronic data with the Community and its Member States. Following the expected nomination of the Independent Regulator in the telecommunications sector his newly established authority should start working soon. An upgrading of the border management in the field of justice and home affairs is imperative. Further efforts are also required in establishing the necessary administrative capacity to ensure the sound, efficient and controllable management of EC funds.

*Overall, the administrative capacity of Cyprus is already largely in place to implement the different aspects of the *acquis*.*

Over the last year Cyprus has met the short-term priorities of its Accession Partnership with regard to free movement of capital, environment and financial control. In most other areas the priorities were partially fulfilled. Cyprus has continued to make progress in addressing the medium-term Accession Partnership priorities, and has partially fulfilled a number of them, such as justice and home affairs, regional policy and co-ordination of structural instruments and issues relating to the internal market."

4.1. The chapters of the *acquis*

As indicated, the following review of Cyprus's ability to assume the obligations of membership has been structured in accordance with the list of 29 negotiating chapters. Accordingly, this section opens with an assessment of progress relating to the cornerstones of the internal market which are known as the "four freedoms", and continues with a systematic review of progress on each of the chapters, covering all aspects of the *acquis*, including sectoral policies, economic and fiscal affairs, regional policy, environment, justice and home affairs, external policies, and financial questions.

Chapter 1: Free movement of goods

Progress since the last Regular Report

Since the last Regular Report, Cyprus has made further progress in the field of free movement of goods, in particular as regards the New and Global Approach Directives and public procurement.

In the area of **horizontal and procedural measures**, Cyprus has adopted certain components of the framework legislation, introducing the New and Global Approach principles into domestic legislation

Important progress has been achieved in the past year as regards the adoption of **sector specific legislation**. The new Framework Law, enacted by the House of Representatives in March 2002, enables the transposition of *New Approach Directives*. Since the last Regular Report, national legislation approximation has been completed in the areas of

dangerous substances and preparations, drug precursors, detergents, pressure vessels (Old Approach Directives) and Wood.

In the areas covered by the *New Approach Directives* the Radio-communication Law, the Basic Requirements (Gas Appliances) Regulations, and the Basic Requirements (Toys) Regulations have been adopted in July 2002. As regards sectors covered by *Old Approach Directives*, some substantial progress was achieved.

In the field of motor vehicles some substantial progress has been achieved with the adoption of framework directives relating to type-approval of motor vehicles.

Regarding foodstuffs, the House of Representatives approved regulations on colouring matters in foodstuffs, on materials and articles in contact with foodstuffs, on control and hygiene of foodstuffs, manufacturing and processing of foodstuff in January 2002. Regulations on labelling of food additives (including provisions relating to the labelling of genetically modified foodstuffs), on processing aids, on foodstuff for particular nutritional uses, and on foodstuffs treated with ionising radiation were enacted in May 2002. In July 2002 regulations were approved on cocoa and chocolate products intended for human production and the hygiene and official control of foodstuffs. Regulations on coffee extracts and chicory extracts, sugar, dehydrated preserve milk, quick frozen foodstuffs, mineral hydrocarbons, foodstuffs intended for particular nutritional uses, cereal based foods, and baby foods were approved in September 2002 (*see also chapter 7 – Agriculture*).

Concerning chemicals, legislation on dangerous substances and preparations and on detergents was approved in June 2002. An order on narcotics and psychotropic substances aiming at aligning with the *acquis* was issued in July 2002.

In the pharmaceutical sector, further transposition has been achieved with the adoption of the Veterinary Medicinal Products Regulations of 2002.

The Weights and Measures Law was approved and entered into force in March 2002, accompanied by seven regulations on weights and measures. Weights and measures regulations on electrical energy meters and taximeters were enacted in July and August 2002 respectively. Furthermore, the Minister of Health has adopted a Decree in November 2001 adopting the Inventory of Ingredients included in Cosmetic Products as published by the Commission and setting the fees for the submission of applications concerning cosmetic products. The Wood in the Rough Law and the Gas Cylinders Law were approved in May 2002, the latter amended again in September 2002.

Since the last Regular Report, progress has been made as regards the **non-harmonised sector**. In the period covered by this report, certain requirements relating to mandatory labelling of country of origin that could be considered as contravening Article 28 of the EC Treaty, were removed by the Trade Descriptions (Amendment) Law of July 2002.

As regards **public procurement** the Act on the Contracts awarded in the Fields of Transport, Water, Energy and Telecommunications was enacted in March 2002 and entered into force in April 2002. This law co-ordinates the procurement procedures of entities operating in the above mentioned fields.

As regards *administrative capacity*, the Standardisation, Accreditation and Technical Notification Law was enacted by the House of Representatives in July 2002 with the

issue of a Ministerial Order. According to this law, accreditation and technical information functions will be undertaken by the Cyprus Organisation for the Promotion of Quality (i.e. the former Cyprus Organisation for Standards and Control of Quality, which has been renamed). The functions of standardisation and certification will be vested with the newly established private company “Cyprus Company for Certification”.

The data base on chemical substances was further enriched with new data collected during the period under review. The capacity of the Department of Labour Inspection has been enhanced through training activities. The Drugs Price Control Committee, which acts as the advisory body to the Minister of Health relating to medicinal products for human use, was appointed by the Council of Ministers in January 2002 and its establishment is provided under the new harmonised legislation. The Department of Pharmaceutical Services of the Ministry of Health was strengthened with the appointment of 4 pharmacists and 1 technician in February 2002. The Veterinary Drug Council acting as the Regulatory Body for Veterinary Drugs was established in June 2002. The Department of Veterinary Services was enhanced through the recruitment of 10 permanent veterinary surgeons and 5 veterinary surgeons on contract. The Council of Ministers has appointed the Cosmetics Council in January 2002 as the competent authority for the regulation of cosmetic products. The Department of Pharmaceutical Services, that has been further strengthened with the recruitment of 1 pharmacist and 1 technician, offers the necessary administrative support for the effective and timely implementation of the decisions taken by the Cosmetic Council.

Overall assessment

Concerning *horizontal and procedural measures*, Cyprus has made progress, but several key aspects, such as interchange of data between administrations, market surveillance, product safety, and safety checks at external borders, or the elimination of all restrictions on the free movement of goods between Member States, have yet to be addressed.

In the area of *sector specific legislation*, in terms of motor vehicles, the adoption of the type approval framework law is a step in the right direction and the Type Approval Authority will be established within 2002.

As regards food safety (*see also Chapter 7 – Agriculture*), considerable efforts are still necessary to speed up the transposition and implementation process.

As regards New Approach Directives, regulations still need to be enacted. Those regulations, which concern product groups such as electrical equipment, machinery lifts, simple pressure vessels, and pressure equipment are before the House of Representatives for approval. In order to achieve full alignment with regard to the pharmaceutical veterinary sector, an additional set of regulations providing for the establishment of maximum residue limits of veterinary medicinal products in foodstuffs of animal origin remains to be approved.

Cyprus continues to make steady progress in the adoption of the *acquis* on industrial products, generally respecting the sections of the government’s Law Approximation Programme for transposition of EC technical regulations into Cypriot law.

As regards *administrative capacity*, it has been decided that the Cyprus Organisation for the Promotion of Quality will undertake the functions of Accreditation whereas the

functions of Standardisation and Certification will be vested with the Cyprus Company for Certification. The implementation of the legislation regarding dangerous substances falls under the responsibility of the Labour Inspection Department of the Ministry of Labour and Social Insurance. The Department of Labour Inspection and the Health Inspection Services need to be further enhanced through additional personnel. Major efforts are required to train food operators to the food hygiene requirements. Investments are being made in the relevant laboratories and control services.

While progress has been made in the accreditation of the State General Laboratory, there is still a need for additional laboratory training and for further upgrading of laboratory facilities to meet the requirements of the *acquis* before accession. On foodstuffs, the level of controls needs to be further increased.

Cyprus is already running a rapid alert system with adequate equipment, which will be further complemented in 2002. To service the system fully, additional human resources would however be necessary and the concerned administrations better co-ordinated to integrate fully the alerts on food and those on feed. As regard novel foods, Cyprus still needs to be adequately prepared to assess them upon accession; Cyprus is in the process of setting up the necessary training and procurement of the laboratory personnel and equipment for the control of genetically modified foodstuffs.

As regards fertilizers, pesticides, pharmaceuticals for human use, cosmetics, footwear, textiles and crystal glass, legislation was already in line with the *acquis* before the last Regular Report. As regards the transposition of the *acquis* on firearms and cultural goods there is still some legislation to be adopted. The acquisition and possession of firearms, weapons, and ammunition is regulated in Cyprus by the Firearms Law, which has to be amended. Also legislation on the return of cultural objects unlawfully removed from the territory of the country and on the export of cultural goods law is before the House of Representatives for approval.

Screening of the Cypriot legislation is ongoing in order to abolish, by accession, all restrictions contrary to Articles 28-30 of the EC Treaty. The Ministry of Commerce, Industry and Tourism will be the administrative entity responsible for the follow-up of the application of Articles 28-30 of the EC Treaty and the implementation of the principle of mutual recognition whose practical implications must be urgently addressed.

In the field of *public procurement* although Cyprus has not achieved full alignment yet with the *acquis* it should be in a position to do so provided the legislative timetable is not further delayed. A draft law is under preparation with the aim of achieving full alignment with the public procurement directives and with the new directive on the mandatory use of standard forms for the publication of contract notices. It is important that the shortcomings noted in the legislation currently in force, which presents substantive gaps and incompatibilities in key areas (concessions, national preference clause), are corrected by the envisaged new legislation. Cyprus should also continue to strengthen its administrative capacity in order to ensure effective application of the public procurement *acquis*.

Regarding the Regulation on the functioning of the internal market in relation to the free movement of goods among the Member States, the Cypriot authorities have appointed the responsible authority for its implementation, which is the Department of Trade within the Ministry of Commerce, Industry and Tourism.

As regards safety checks on products at external borders, administrative co-operation arrangements set up between customs and market surveillance authorities in this area still need to be assessed.

Conclusion

In its 1998 Regular Report, the Commission concluded that Cyprus had made progress in the transposition of the *acquis* in the field of free movement of goods, but further efforts to transpose the *acquis* were needed. Substantial work remained to be done and special attention should be paid to implementation and enforcement structures.

Since the 1998 Regular Report, substantial progress has been achieved and approximation has been completed in a number of sector specific areas but administrative capacity needs further enhancement. Regarding New Approach Directives, following an initial delay in transposition, progress has taken place with the enactment of the New Framework Law, Regulations, and the enactment of the new Law on Standardisation, Accreditation and Technical Notification. Cyprus is at an advanced stage in terms of transposition and administrative capacity in the field of free movement of goods.

Negotiations on this chapter have been provisionally closed. Cyprus has been granted a transitional arrangement for the renewal of marketing authorisations for medical products (until 31 December 2005). Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, efforts are required as regards the implementation of the mutual recognition principle. Renewed efforts are necessary to meet to objective of full transposition/implementation of the food safety *acquis* by the date of accession. Also the enhancement of the administrative infrastructure needs to be continued in the areas of accreditation, testing and certification.

Chapter 2: Free movement of persons

Progress since the last Regular Report

Since last year's Regular Report, Cyprus has made good progress regarding alignment with the *acquis* or establishment of the required administrative structures.

In the field of **mutual recognition of professional qualifications**, the General System for Recognition of Professional Qualifications Law has been approved in September 2002. This framework law aims at transposing the first General System Directive and stipulates in line with the above directive the appointment of a National Co-ordinator. Progress has also been achieved with respect to legislation aiming at transposing sectoral directives; in this respect legislation concerning the professions of lawyers, veterinary surgeons, and pharmacists has been adopted in September 2002.

In the area of **citizens' rights** and **free movement of workers**, no legislative developments can be reported.

Preparatory work has continued to facilitate Cyprus's participation in the European Employment Services system (EURES).

Concerning **co-ordination of social security systems**, Cyprus has continued to apply its bilateral social security agreements with Member States, which normally rely on the same principles as the Community rules in this field. This process familiarises the administration with the procedures. A law amending the social insurance legislation to comply with the relevant *acquis* in relation to the right to voluntary insurance and the payment of sickness, unemployment, maternity and accident at work benefits outside Cyprus was enacted in July 2002. The House of Representatives has approved 65 new posts for the Department of Social Insurance in July 2002.

To enhance *administrative capacity* in all areas various study visits and seminars have taken place.

Overall assessment

As regards mutual recognition of professional qualifications, Cyprus has advanced considerably. However, Cyprus still has to adopt outstanding sectoral legislation (on architects, doctors, dentists, pharmacists, nurses, and midwives) as well as a law transposing the directive on a second general system for the recognition of professional education and training. The recently approved framework law stipulates the appointment of a National Co-ordinator for the activities of the various competent authorities and for promoting uniform application of the general system directives. Its compliance with the *acquis* needs further assessment. By accession, it has to be ensured that all Cyprus's legislation is aligned with Community rules, in particular with respect to nationality, residence and language requirements. Legislation needs to be monitored to ensure that it distinguishes between academic and professional recognition and includes simpler procedures to allow for the provisions of services.

As regards citizens' rights, preparatory legislative work is advanced. It is important that the envisaged new legislation on voting rights, in particular relating to the European Parliament elections, will be adopted as foreseen. In tertiary education the elimination of certain existing discrepancies with regard to fees has to be continued in order to ensure equal treatment between Cypriot and EU nationals.

With respect to the free movement of workers, Cyprus has to enhance its approximation efforts so that the necessary legal and practical framework is in place upon accession. Preparatory work for the approximation and implementation of legislation has continued but needs to be reinforced. Envisaged legislation aimed at aligning with the *acquis* on the right of free movement of workers and residence of the nationals of the Member States and of the members of their families' needs to be enacted. Attention should focus on ensuring that by accession Cypriot legislation respects the principle of non-discrimination.

As regards full participation in EURES, preparations should continue, in particular with regard to language training.

Concerning the co-ordination of social security systems, further work to develop the necessary administrative structures, in particular a substantial reinforcement of staff and training, is needed.

Concerning administrative capacity, the approved recruitment of 65 additional staff was an important step towards strengthening administrative capacity. Relevant EU-related

training of staff is required urgently to put the Cypriot administration in a position to deal with the new challenges faced with regard to the *acquis* in the area of mutual recognition of professional qualifications, free movement of workers and co-ordination of social security schemes.

Conclusion

In its 1998 Regular Report, the Commission concluded that further efforts to transpose the *acquis* would be needed and that special attention would have to be paid to implementation and enforcement structures.

Since the 1998 Regular Report, Cyprus has continued to undertake measures for further harmonisation with the *acquis* in the field of free movement of persons. It has abolished inconsistencies as regards the co-ordination of social security systems and has approved legislation granting the mutual recognition of qualifications. The alignment with the *acquis* is at an advanced stage. Cyprus has reached a good level of administrative capacity to implement the *acquis* in this field.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangement. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on the adoption of outstanding legislation on the mutual recognition of qualifications (second General System Directive and sectoral legislation on architects, doctors, dentists, pharmacists, nurses, and midwives), on the right of free movement of workers and residence of the nationals of the Member States and the members of their families, and on voting rights.

Chapter 3: Freedom to provide services

Progress since the last Regular Report

Since last year's Regular Report, Cyprus has made good progress in terms of harmonisation, although further alignment is needed.

In the field of **the right of establishment and the freedom to provide non-financial services**, Cyprus has recently taken measures to progress on the liberalising of foreign direct investment from EU Member States.

In the field of **financial services**, with regard to the *banking sector*, the *administrative capacity* of the Central Bank has been strengthened. The Central Bank's Banking Supervision and Regulation Division has recruited 4 additional officers and 5 administrative assistants. The Public Administration and Personnel Service has approved the posts of eight additional officers for the Department of Co-operative Development, which is responsible for supervising the Co-operative Credit and Savings Societies (CCSSs).

As regards the *insurance sector* Cyprus has passed a new law to achieve compliance with the *acquis*, the Insurance Services and Other Related Issues Law of 2002, which was enacted in April 2002 and will enter into force in January 2003. Provisions relating to the

single passport and home country control principles have been incorporated in the new law and will come into force upon accession.

The *administrative capacity* of the Insurance Companies Control Service (ICCS) of the Ministry of Finance has been enhanced. Also the implementation of the ICCS Information Systems Strategy has been initiated.

In the field of *investment services and securities markets*, there has been further progress in terms of harmonisation. An amending law and regulations were approved by the House of Representatives in June 2002, in order to introduce a number of changes to the Securities and Stock Exchange of Cyprus Laws and regulations, bringing them into compliance with the EC directives. This legislation includes the required amendments to permit citizens and legal entities from EU Member States to become members of the Cyprus Stock Exchange, to enable banks to act as brokers, to enable the Cyprus Stock Exchange to co-operate and exchange information with other competent authorities and to put in place the provisions for mutual acceptance of prospectuses and recognition of home state supervision which will become effective upon accession.

A Bill on Investment Services was enacted in July 2002. It covers the Investment Services Directive, the Capital Adequacy Directive, and the Investor Compensation Directive. Regarding the issue of mutual acceptance of home member authorisation, the right to provide services in one Member State for firms established in another and the right of the home state to require information from the host state, and the issue of the acceptance of Member State investor compensation schemes substituting in part or in full for host country schemes, relevant provisions are incorporated in the legislation which will become effective upon accession. Also a Law providing for the Requirements for the Undertaking of an Invitation to the Public for Investment in Financial Instruments and Other Related Measures was enacted in July 2002.

The Insider Dealing Law was amended in early 2002 to enable the Securities and Exchange Commission to submit regulations and to change the definition of the “closed period” so as to close a gap that existed for abuse. In early 2002 the Stock Exchange Regulations were amended to introduce the requirement of the application of International Accounting Standards on the six-month periods for issuers and the dissemination of specific information within specific periods.

The Cyprus Stock Exchange has implemented the automated central depository and central registry (CSD) as from July 2001. As of January 2002, the securities of 39 listed companies out of a total of 150 listed companies are held in the CSD. With the implementation of the CSD, the Cyprus Stock Exchange is working on an online trading, clearing and settlement process for these companies.

Concerning the **protection of personal data and the free movement of such data**, Cyprus ratified in February 2002 Convention 108 of the Council of Europe. The Data Protection Act was adopted in November 2001. The Office of the Commissioner for Personal Data Protection has been set up and the Commissioner was appointed in March 2002. The office currently has three highly qualified officers to assist the Commissioner and three support staff. These posts so far are temporary ones (*see chapter 24 – Co-operation in the field of justice and home affairs*).

As regards **information society services**, Cyprus has ratified the European Convention on the Legal Protection of Services, based on, or consisting of, Conditional Access in July 2002.

Overall assessment

Cyprus's legislation still includes certain restrictions which have to be removed.

A bill amending the Immovable Property Acquisition (Aliens) Law is still to be adopted. Legislation to achieve compliance with the requirements of the directives and regulations concerning the right of residence is also still to be completed. Cyprus still needs to lift restrictions on real estate agents, electricity, press, and travel offices and tertiary education.

Cypriot banking legislation is largely in line with the *acquis*. The prudential rules of the Central Bank of Cyprus, which is the authority responsible for regulating and supervising banks, are largely based on the recommendations of the Basle Committee on Banking Supervision and the EC Directives on credit institutions. The Banking Law of 1997 and its subsequent amendments provide the legal framework for the conduct of banking business and the prudential rules. It is currently being reviewed with the aim of introducing certain amendments that will bring the legal framework into line with the EC banking *acquis* by the end of 2002. The new Directives on contractual netting agreements and electronic money institutions are still to be enacted. The deposit guarantee scheme has to be enacted to cover foreign currency deposits.

Regarding the CCSSs, legislation incorporating all outstanding relevant provisions of the *acquis* on credit institutions is still to be completed.

The responsible division in the Central Bank appears to have the required administrative infrastructure and the necessary human resources to ensure the effective implementation and enforcement of the *acquis* in the area of banking.

There is close co-operation between the Department of Co-operative Development and the Central Bank so as to ensure that comparable standards of supervision are applied. Measures are underway for the full computerisation of all CCSSs as well as the upgrading of the electronic systems, so as to enhance the off-site monitoring capacity of the Department of Co-operative Development by January 2003.

In the *insurance sector*, supervision is performed by the ICCS of the Ministry of Finance, which needs additional human resources to permit more effective implementation of the *acquis*. The fourth motor insurance Directive still has to be transposed. Legislation on annual accounts and consolidated accounts, as well as on initial public offerings, remains pending.

In the field of *investment services and securities markets*, Cyprus is broadly in line with the *acquis*. A bill dealing with the requirements of the Investment Services Directive, the Capital Adequacy Directive, the Investor Compensation Directive, initial public offerings and collective investment services has now been enacted. Further efforts are required in this area. In view of the well developed market for offshore investment funds the proper implementation of the Undertakings for Collective Investment in Transferable Securities Directive is a matter of priority.

With respect to the issue of strengthening supervision, there is some further need to delineate the responsibilities and powers of the Securities and Exchange Commission and the Cyprus Stock Exchange. Correct and effective supervision requires that the supervisor is completely independent. The Securities and Exchange Commission also needs additional staff. Further resources should be made available to the supervisory authorities in charge of credit co-operatives and insurance supervision.

As regards the *protection of personal data and the free movement of such data*, the legislation is largely in line with the *acquis* and the necessary administrative capacity is being put in place. The Data Protection Commissioner is appointed by the Council of Ministers for a four-year term. The Commissioner cannot be dismissed during this period except for reasons of mental or physical incapacity or physical handicap. The Commissioner has his/her own budget and has recruited personnel for an effective exercise of his/her duties.

Cyprus still needs to transpose the E-Commerce Directive and the Transparency Directive.

Conclusion

In its 1998 Regular Report, the Commission concluded that since the 1993 Opinion Cyprus had made progress in the transposition of the *acquis* in parts of the general framework and the fields of services. Further efforts to transpose the *acquis* were needed and special attention would have to be paid to implementation and enforcement structures. The fact that the legal provisions for the operation of the important offshore sector could be incompatible with the *acquis* raised particular concerns. In particular offshore financial activities did not seem to be entirely compatible with the prevailing banking legislation.

Since the 1998 Regular Report, Cyprus has made good progress, in particular with the new Law on Insurance Companies as well as with the amendment of the Banking Law in 1999 through which offshore banks are subject to the same regulatory and supervisory regime as domestic banks. In the field of the *right of establishment and freedom to provide services* possible remaining restrictions in the Cypriot legislation need to be removed before accession. However, legislation is to a good extent aligned. Cyprus has reached an adequate administrative capacity to implement the *acquis* in this field.

Negotiations on this chapter have been provisionally closed. Cyprus has been granted a transitional period (until 31 December 2007) in which to ensure the full application of the *acquis* in respect of co-operative credit institutions. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts in the banking field now need to focus on the implementation of the contractual netting Directive and on the need to abolish the economic need criterion in preparation for the adoption of the "single passport" principle. Enhancement of administrative capacity should continue in the field of financial services, in particular as regards supervisory authorities. In the securities field there are several aspects where harmonisation still has to be completed. Furthermore regulations are needed on the provision of information in the field of technical standards and regulations. The Co-operative Central Bank, which will be the central body for the permanent affiliation arrangements, will have to be operational in good time.

Chapter 4: Free movement of capital

Progress since the last Regular Report

Since the last Regular Report, Cyprus has made progress at a moderate pace in this chapter. The liberalisation of capital movements has continued and is still on course to achieve a progressive transition upon accession.

In the field of **capital movements and payments**, Cyprus increased ‘allowances’ concerning capital movements. With regard to investments in real estate, as of January 2002 the limit on the amount each resident family may transfer abroad to acquire a secondary residence was raised to CY£ 200,000 (€ 347,222). From September 2002 on each resident natural person may transfer abroad up to CY£ 50, 000 (€ 86,805) annually to purchase securities listed on stock exchanges in EU member states or units of enterprises for collective investment in transferable securities (UCITS). Alternatively, part or this entire amount may be deposited in accounts with foreign banks. In January 2002 the limit on cash withdrawals abroad by residents through credit or debit cards issued by domestic banks was raised to CV£ 1,000 (€ 1,736) per trip. As from September 2002 the limit of CY£ 50,000 (€ 86,805) on the amount of gifts or endowments granted by resident parents to each of their non-resident children was abolished and at the same time the limit on other gifts or endowments by residents to non-residents was increased to CY£ 2,000 (€ 3,472) every six months. As from September 2002 direct investment projects have no longer to be referred to the Central Bank of Cyprus for verification of genuineness except projects necessitating the transfer of funds in excess of CY£ 5,000,000 (€ 8,680,555) per annum.

As far as direct investments in Cyprus by non-residents are concerned, the removal of restrictions on telecommunications and postal services was adopted by the Parliament in March 2002, but parts of it will only enter into force on a date specified by regulations issued by the Council of Ministers and submitted to the House of Representatives for approval, at the latest by January 2003.

In the field of **payment systems (cross-border credit transfers)** no particular legislative developments can be reported.

As regards **the prevention of the use of the financial system for the purpose of money laundering**, the Council of Ministers appointed in December 2001 the Central Bank of Cyprus as the Supervisory Authority for persons and entities who offer money remittance services and draft guidance notes for these persons/entities have been finalised. In March 2002 a new guidance note was issued, which defines who are to be considered principal beneficiary shareholders, provides for the obligation for banks to identify the persons who have ultimate control over a company’s business and assets, irrespective of the percentage they hold in the company, and introduces a new procedure for the identification and monitoring of accounts of politically exposed persons. As regards administrative capacity a new reporting system for balance of payments transactions was implemented in January 2002. As far as the enhancement of the administrative capacity of the Unit for Combating Money Laundering (MOKAS) is concerned, 11 posts were created for the Unit for Combating Money Laundering (MOKAS) of which 2 were for lawyers, 8 investigators (accountants and financial analysts) and one

support/administrative staff. Recruitment started in July (*see also Chapter 24 - Co-operation in the field of justice and home affairs*).

Overall assessment

In the field of capital movements, liberalisation in line with the *acquis* has continued and must now be completed before accession. Efforts in this field must continue to ensure the proper functioning of the markets from the date of accession. Concerning direct investment by non-residents, sector specific restrictions i.e. in the sectors of electricity and tourism and travel offices remain to be abolished and legislation amending the Press Law needs to be adopted. An amendment of the Tertiary Education Schools Law, that eliminates the existing distinction between Cypriot citizens and citizens of the EU member-states concerning the establishment of tertiary education schools in Cyprus is undergoing legal vetting and needs to be adopted. A bill amending the Immovable Property Acquisition Law has been approved by the Council of Ministers and will be submitted to the House of Representatives for enactment. The law will liberalise investments in real estate in Cyprus by EU natural and legal persons by accession, the only exception being the acquisition of secondary residences, for which a transitional period has been granted. As regards payment systems, efforts are still needed in terms of alignment with the *acquis*. The Cross-Border Credit Transfers and the Settlement Finality Directives as well as Recommendations on electronic payment instruments are yet to be fully transposed in Cyprus. In terms of administrative capacity Cyprus still needs to establish an out-of-court redress scheme to deal with the settlement of complaints between banks and their customers. Necessary infrastructure in relation to payment and securities' settlement is now in place.

As regards money laundering, Cyprus has implemented all the necessary legislation in this area and put in place the necessary administrative capacity. However, further progress is still expected in terms of completing the reinforcement of the administrative structure of the Unit for Combating Money Laundering (MOKAS) with the recruitment of the approved additional staff, which was started in July, and through simplification of procedures, enhancement of training and improved co-operation between MOKAS police and state prosecutors. According to the Ratification Law of the U.N. International Convention on the Suppression of the Financing of Terrorism, the offences prescribed in the Convention are considered to be "predicate offences", thus the relevant provisions of the Prevention and Suppression of Money Laundering Activities Law of 1996, as amended, directly apply (e.g. freezing order, confiscation etc.). Moreover, with a specific section of this Law, the investigation of such offences is assigned to MOKAS, where a special section to deal with information related to the financing of terrorism will be set up.

Conclusion

In its 1998 Regular Report, the Commission concluded that since the 1993 Opinion Cyprus had made progress in the transposition of the *acquis* in parts of the general framework and the field of free movement of capital, but further efforts were needed. Special attention would have to be paid to implementation and enforcement structures. The capital markets regime had a considerable distance to go to approach the *acquis*. Special attention would have to be paid to implementation and enforcement structures.

Since the 1998 Regular Report, Cyprus has made steady progress, both in aligning its legislation and in developing the necessary administrative structures. Cyprus is at an advanced stage in terms of legislative alignment and administrative capacity in the field of free movement of capital.

Negotiations on this chapter have been provisionally closed. Cyprus has been granted a transitional period for five years from the date of accession for the acquisition of secondary residences. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on completing alignment and eliminating all remaining restrictions, completing the administrative structures necessary to implement the *acquis* in this area, and reinforcing administrative capacity. It must pay particular attention to the bodies involved in the fight against money laundering, complete the recruitment of additional staff for MOKAS and continue sustained efforts in particular in relation to the offshore sector.

Chapter 5: Company law

Progress since the last Regular Report

Since last year's Regular Report, Cyprus has made further progress in the areas of company and accounting law and the protection of intellectual and industrial property rights.

Concerning **company law** as such, in order to intensify the computerisation process of the Companies Register, four clerical and auxiliary staff joined the Department of the Registrar of Companies and Official Receiver in June 2002 in order to intensify the computerisation process of the Companies Register.

With regard to **accounting**, the Council of Ministers approved in February 2002 the Institute of Certified Public Accountants as the competent regulatory body of the profession, which is responsible for granting approval to qualified persons for carrying out the statutory audits of accounting documents.

In the field of **protection of intellectual and industrial property rights**, the House of Representatives enacted a bill amending the Cyprus copyright law in July 2002. The legislation plays a crucial role in the alignment process as it aims at implementing the Directives on software protection, rental and lending rights, and the term of protection and database protection, including the *sui generis* right.

The amendment of the Cyprus Patent Law enacted in July 2002 aims at aligning with the Directive on the legal protection of biotechnological inventions.

The Legal Protection of Industrial Designs and Models Law and the Legal Protection of Topographies of Semiconductor Products Law were enacted in January 2002 and came into force in February 2002. Also, new legislation on counterfeit and pirated goods was enacted in April 2002 with the Control of Movement of Goods Infringing Intellectual Property Rights Law. With regard to the strengthening of law enforcement capacity to combat piracy and counterfeiting, control at border points (for exports and imports) has been introduced, in accordance with the provisions of the above-mentioned Law. Staffing

has been increased in this field and training has been carried out to be able to cope with the new tasks provided for by the new Law.

There were 22 seizures of counterfeiting and pirated goods performed at the border for the protection of intellectual and industrial property rights, with a total value of CY£ 12,487 (€ 21,687) in 2001.

The WIPO Copyright Treaty was ratified in July 2002. The ratification enhances the legal framework for the protection of works in digital form.

As regards the **Regulation replacing the Brussels Convention** on jurisdiction and enforcement of judgements in civil and commercial matters and the **Rome Convention** on the law applicable to contractual obligations, preparatory work for swift implementation continues.

Overall assessment

Cyprus must urgently adopt legislative amendment to fulfil the requirements of the Second (co-ordination of safeguards), Third (mergers), Fourth (annual accounts), Sixth (divisions of public limited companies) and Eleventh (disclosure requirements) Directives. Cyprus's legislation is to a large extent in line with the *acquis* on accounting law. In accordance with the Companies (Amendment) Law, which provides for the self-regulation of the profession, only members of this certified public accounting body are entitled to perform audits of annual accounts of companies or consolidated accounts of companies. Furthermore, this arrangement covers various aspects of the accounting profession and includes for example disciplinary control, the carrying out of examinations to assess professional competence, and setting the standards for required experience and professional ethics.

The computerisation process of the Companies Register is at an advanced stage, to allow for the effective application of the First Directive, and should be finalised by the end of 2002. Computerisation within the Department of the Registrar of Companies and Official Receiver needs to be finalised and operated properly, and the requested additional members of staff need to be recruited and trained

As regards the *protection of intellectual and industrial property rights*, legislative measures are needed, in particular as regards certain aspects of Copyright and Neighbouring Rights, to comply with the Directive on Copyright in the Information Society and with the Directive on Resale Rights. Some additional adjustments of trademark legislation will be necessary upon accession.

Cyprus suffers from a high level of piracy, notably in the area of videos and CDs. In 2001, the proportion of pirated music products was estimated (by industry) at 47%. This makes it essential for Cyprus to concentrate its fight against piracy and counterfeiting. Furthermore co-ordination and co-operation between the various institutions/administrative bodies responsible for intellectual and industrial property rights (IPR) need to be enhanced. Further efforts are required to strengthen law enforcement capacity as regards border controls and combating piracy and counterfeiting. Targeted training of all services involved in the implementation and enforcement of IPR legislation, necessary for both IPR officials and for enforcement officials, including judges and prosecutors, should remain an important task.

Concerning the *Regulation replacing the Brussels Convention* on jurisdiction and enforcement of judgements in civil and commercial matters and the *Rome Convention* on the law applicable to contractual obligations, the Government continues to be in close contact with the judiciary for the designation of the relevant courts which will have to deal with applications and appeals (*see also Chapter 24 - Co-operation in the fields of justice and home affairs*).

Conclusion

In its Regular Report of 1998, the Commission concluded that the Cypriot company law of 1951 had been amended several times with a view to aligning with the *acquis*, but that further approximation was needed on a number of aspects. Important progress had been made in recent years, in particular, on industrial property rights.

Since 1998, Cyprus has made steady progress in terms of legislative harmonization under this chapter. Transposition in the field of industrial and intellectual property rights is continuing at a steady pace. As regards Cyprus's company law as such, the alignment with the *acquis* is at an advanced stage, even though some discrepancies still remain. Cyprus has reached an adequate administrative capacity to implement the *acquis* in this field.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. It has agreed to the EU proposal related to industrial property rights for pharmaceutical products and Community Trademark. Cyprus is generally meeting the commitments it made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on ensuring full alignment with the *acquis* along the lines set out above. In particular, further legislative measures are needed to comply with the Directive on Copyright in the Information Society and the Directive on Resale Rights. Also the enforcement of intellectual and industrial property rights legislation and the fight against piracy and counterfeiting must continue to be a priority. In this respect, the work of the administrative and judicial bodies involved in enforcement, such as the customs services, the police and the judiciary, must be strengthened, including co-ordination among them.

Chapter 6: Competition policy

Progress since the last Regular Report

Since the last year's Regular Report, Cyprus has made further progress in this area.

In the **anti-trust** field, with respect to implementing legislation, Cyprus has introduced most of the necessary legislation corresponding to Community block exemptions, including the Community's new policy on horizontal and vertical restraints. A leniency programme was also adopted.

Cyprus submitted an "Action plan for strengthening the administrative capacity of the Commission for the Protection of Competition" to the Commission in April 2002.

The Commission for the Protection of Competition (CPC) has continued to build on its enforcement record over the past year. In 2001, the CPC issued 25 decisions in anti-trust cases whereof two conditional approvals. Recently it has started a pro-active approach including own-initiative investigations. It has also made an effort to start a more deterrent sanctioning policy, including the imposition of substantial punitive fines

In the field of **state aid**, Cyprus adopted implementing legislation concerning sales of land and buildings, and national regional aid. A circular attaching the Commission notice on the application of the state aid rules to measures relating to direct business taxation has been addressed to the appropriate authorities. As of January 2003 all fiscal aid will be subject to state aid control. A regional aid map, which is in line with the *acquis*, was agreed with the European Commission in April 2002.

The state aid survey for 2000 was completed in January 2002 and follows the methodology and presentation of the “Survey on State Aid in the European Union”.

The national state aid monitoring authority is the Office of the Commissioner for Public Aid. It is headed by an independent official, the Commissioner for Public Aid, who was appointed in May 2001. Its enforcement record in the field of state aid has emerged. By September 2002, the CPA had issued a total of 122 decisions in the period covered by this report.

Overall assessment

As regards anti-trust regulations, the overall assessment is positive with some further efforts required. Alignment of legislation is well advanced.

The CPC is a fully independent authority. It has broad powers to enforce competition rules. It is staffed by nine officials (in addition to five supporting staff). Further training efforts and strengthening of the Commission for the Protection of Competition is necessary and measures are underway. It is understood that the CPC will continue to actively develop its resources, in particular in view of the planned modernisation and decentralisation of the application of the EC anti-trust rules. The recent development of the anti-trust enforcement record of the Commission for the Protection of Competition is satisfactory. Cyprus should however develop it further. In the area of anti-trust the most important challenge is to ensure the effective application and enforcement of the anti-trust rules. A more deterrent sanctions policy is needed. Priority should also be given to cases involving the most serious distortions of competition, including the effective application and enforcement of the anti-trust rules to sectors where the continuing existence of statutory monopolies and administrative orders regulating trade in certain goods prevents the normal application of competition rules. Increase awareness raising of the rules is important, not least in relation to the business community and the judiciary.

As regards state aid, the overall assessment is positive. The Public Aid control law of 2001 contains the main principles of State aid control. As for implementing legislation, the essential *acquis* has been implemented. The Office of the Commissioner for Public Aid is functioning well. At present, there are seven people working in this office. The enforcement record includes 33 negative decisions, 49 conditional approvals and 21 approvals, whereas in 19 cases the CPC decided that the measure did not constitute a state aid. Cyprus should continue to ensure the effective application and enforcement of the rules.

Conclusion

In its 1998 Regular Report, the Commission concluded that the legislative situation as regards anti-trust aspects of competition in Cyprus was generally encouraging. Work was needed on enforcement. Merger control needed to be established. Rules similar to Article 90 of the EC Treaty were to be adopted quickly. In order to ensure effective enforcement of competition rules, efforts needed to be made to reinforce the Office for the Protection of Competition. Further specialised training would be essential. Monopolized sectors should be adjusted. In the State aid area, the adoption of the legislative framework would need special attention.

Since 1998, Cyprus has made steady progress in adopting anti-trust legislation and has developed the Commission for the Protection of Competition's administrative capacity. The anti-trust enforcement record has improved. Steady progress has also been made in adopting state aid legislation. The State Aid Monitoring Authority has been established and functions well. Overall, on legislative alignment, administrative capacities and enforcement record Cyprus is reasonably advanced.

Negotiations on this chapter have been provisionally closed. Cyprus has been granted a transitional arrangement by which international offshore companies, which were in business on 31 December 2001, will continue to be taxed at a lower rate than the normal rate of corporation tax until 31 December 2005. Cyprus is generally meeting the commitments taken and the requirements for sufficient legislative alignment, administrative capacity and enforcement record, arising from the negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on ensuring that it continues to update its alignment as the *acquis* in this area evolves and, most importantly, on continuing to develop a track record of proper application and enforcement of both anti-trust and state aid legislation.

Chapter 7: Agriculture

Progress since the last Regular Report

Since the last Regular Report, Cyprus has made steady progress in the area of agriculture, both with aligning legislation and with strengthening administrative capacity.

Agriculture in Cyprus accounted for 3.9% of gross value added in 2001 compared with 3.7% in 2000²³. Employment in agriculture has declined considerably over recent years, and now accounts for 4.9% of total employment²⁴.

In 2001, overall agricultural trade²⁵ between Cyprus and the EC showed mixed tendencies. EC imports of agricultural products originating in Cyprus increased by 6% to

²³ The source for all agricultural statistics is EUROSTAT unless otherwise specified.

²⁴ Data for the years 1999-2001 based on largely EC-harmonised Labour Force Survey definitions (LFS) data collected in the second quarter of each year (April-June). Agricultural employment is defined in LFS terms as economically active persons who gain a significant part of their income from agriculture.

€ 107 million EC exports to Cyprus decreased by 19% to € 266 million in 2001. The trade balance in favour of the Community amounted to € 159 million compared to € 229 million in 2000. EC imports were dominated by fruit and nuts and vegetables. Tobacco, beverages, spirits and vinegar, miscellaneous edible preparations, preparations of cereals, flour, starch or milk and dairy products were the main export goods from the EC.

Horizontal issues

Since last year's Regular Report, Cyprus has made some progress on implementing measures related to the *European Agricultural Guidance and Guarantee Fund (EAGGF)*. The Council of Ministers appointed in March 2002 the Minister of Agriculture, Natural Resources and Environment as the competent authority for the accreditation of the Paying Agency of Cyprus. An inter-ministerial committee adopted the Department of Agriculture's proposals concerning the integration of the functions of the Paying Agency within the Department's structure. A detailed timetable for the functioning of the Paying Agency by the time of accession was submitted in April 2002. The timetable provides that the legislation setting up the Paying Agency along with a Master Plan for the necessary re-organisation and strengthening of the Department of Agriculture and the accreditation of the Paying Agency is to be put in place by June 2003 at the latest. However, the draft legislation setting up the Paying Agency is not yet completed. Meanwhile an expert on Paying Agencies has been recruited in order to review the preliminary Master Plan and make recommendations on the proposed structure. Recruitment of the first 30 officers was completed by the mid-July 2002, whilst a supplementary budget, which was approved in April 2002, provides for another 20 professional and 30 technical staff, who are due to be recruited by the end of the year 2002.

Little progress has taken place as regards the effective implementation of the Integrated Administration and Control System (IACS). A working committee has been appointed to identify and analyse the business processes involved in IACS. In early 2002, a new consultancy was commissioned for the review of the procedures and business processes that the IACS software will support, and also to review and verify the technical specifications of the necessary software systems for the establishment of the required databases and the execution of the necessary data checks and controls. The acquisition of computer hardware and software as well as the training of personnel in Geographic Information Systems (GIS) are provided for in the budget of 2003.

Cyprus considers that its cadastre is reliable and up to date and is therefore suitable to be the basis for the building of its land parcel identification system (LPIS), each cadastral parcel having already a unique identification number. Systematic on the spot controls are planned to be organised in 2002 and 2003 in the framework of the national schemes for cereals in order to check the accuracy of the cadastre and in particular of the area recorded.

Cyprus has decided to use satellite images in order to create a Geographical Information System (GIS) in order to comply with the requirements of the *acquis* but has not yet taken the decision regarding the methodology to be used (block, *îlot* or parcel).

²⁵ Source of trade figures: WTO definition of agricultural products, figures from EUROSTAT COMEXT (see U.E.12/15: Commerce de produits agricoles 1998-2000, 1 Partie D.G.AGRI / G.2 Analyses quantitatives, prévisions, statistiques, études, 2001, pages 10-57 et 86-89).

Regarding *trade mechanisms*, preparation work is continuing.

As regards *quality policy*, the House of Representatives approved the Regulation for the Quality Standard for the export of walnuts in shell in May 2002. The Quality Control of Agricultural Products Law and its relevant Regulations have been enacted in September 2002. Furthermore, a new Law on Producer Organisations has been passed.

In the field of *organic farming* the national Law and its relevant Regulations on Organic Farming were enacted and entered into force in December 2001.

As regards *farm accountancy data network (FADN)* no new developments are to be reported.

Common market organisations

Since last year's Regular Report, Cyprus has made further progress as regards the legislative framework and the administrative structures for the establishment of Common Market Organisations.

As regards *arable crops* the results of the study on the potential alternative roles of the Cyprus Grain Commission (CGC) after the abolition of its monopoly, which is scheduled to be completed by January 2003, have been evaluated by the CGC's Board of Directors. A follow up study based on the recommendations of the initial study has been completed and the CGC decided to proceed with its transformation into two separate companies. One to continue dealing with the trade of cereals in an open market situation and under free competition and a second one to provide storage services that will be available to both the trading company and the private sector on an equal basis. Cyprus has reduced the guaranteed price paid to grain producers and has introduced an area-based payment for cereals, fodder crops and grain legumes, similar to EC schemes. It has been decided that the intervention function should be under the responsibility of the company in charge of providing storage services. The management of import and export licenses will be allocated to the Ministry of Commerce.

In the field of *specialised crops*, Cyprus is working towards the creation of its olive oil registry and all applications had been received by the end of 2001 (declaration of the number of trees per cadastral parcels). Cyprus has also adopted regulations in order to harmonise its legislation for wines, spirit drinks, sparkling wines, liqueur wines and aromatised wines. Enforcement of these regulations is due before accession.

As regards *fruit and vegetables*, Cyprus has indicated it will recognise the producers' organisation and abolish the monopolistic elements of the Cyprus Potato Marketing Board and the Cyprus Carrot and Beetroot Marketing Board. Legislation on quality control was enacted in July 2002.

In the field of *animal products*, as regards the milk industry, in February 2002 the Council of Ministers decided on the abolition of the monopoly powers of the Cyprus Milk Industry Organisation (CMIO). CMIO's human and other resources will be utilised in setting up the competent authorities to undertake the implementation of the *acquis* in the dairy sector, under the Paying Agency. The option of maintaining CMIO as a semi-government organisation with certain functions delegated to it by the Paying Agency is still being examined. With regard to *beef and veal*, a new framework legislation entitled "The Carcass Classification of Bovine, Pig and Ovine Animals and the Reporting of their

Prices Law” and its implementing regulations, introducing a system of compulsory carcass classification and regulating certain aspects of price collection and reporting for beef meat, was enacted in April 2002. Under the before-mentioned framework law, implementing regulations introducing a system of compulsory carcass classification and defining the standard quality of fresh or chilled meat of sheep and pig meat according to Community rules were approved in April 2002. Harmonised legislation on the production, grading, labelling and marketing standards for poultry meat entered into force from October 2001. An updating amendment of both the basic Law and the implementing Regulations was enacted in April 2002.

Rural development and forestry

Cyprus has prepared its code of Good Agricultural Practice, as part of preparations for EC-funded rural development programmes. The Department of Agriculture, together with other relevant ministries, is currently preparing the draft Rural Development Plan.

As regards **rural development and forestry**, the Code of Good Agricultural Practice should enter into force, programming and implementation capacity should continue to be built up and progress should be maintained on the preparation of the Rural Development Plan. The National Forest Programme covering the period 2000-2009 was approved in February 2002, aiming at the protection, management and sustainable development of the country’s forests. The Programme seems to be in line with the *acquis*. The data from the 15 Level I plots for the year 2001 have been made available to the Commission.

Veterinary and phytosanitary issues, including food safety

Since the last Regular Report, progress has been made in transposing and implementing the *acquis* in the **veterinary sector**.

The veterinary public health sector is now covered by two Framework Laws, the Hygiene and Trade of Food of Animal Origin Law (2002) and the Food Control and Sale Law (2001). Concerning the agri-food establishments, the Cypriot Government has decided at the end of 2001 that establishments have to upgrade and comply with the *acquis* or stop operation. The national upgrading plan will be evaluated in autumn 2002 as well as in March and September 2003.

As from 1 September 2002, the Contagious Disease of Animals Law was replaced by the Animal Health Law.

The construction of the Border Inspection Posts (BIP) at Larnaka airport has been completed and the Post is now in operation.

Cyprus joined the computerised network linking veterinary authorities ANIMO in March 2002. The system is in operation on a voluntary trial basis. The Veterinary Services have been connected with the Animal Disease Notification System (ADNS) since January 2002.

Contingency plans for Newcastle Disease, Avian Influenza, Bluetongue, BSE and Scrapie have been completed and submitted to the FVO and TAIEX for evaluation in May 2002.

The application and issue of passports to bovine animals and the individual identification of sheep and goats have started in summer 2002.

Concerning the setting up of the porcine data base progress has been made.

The Department of Agriculture has now recruited 2 more feedingstuffs inspectors. As regards zootechnics the legislation on Animal Improvement Law and implementing regulations were put into force in January 2002. Relevant ministerial Orders have also been prepared, approved and enforced. The staff of the Department of Veterinary Services of the Ministry of Agriculture, Natural Resources and Environment which assumes the responsibility for veterinary matters related to consumer health protection has been increased: 10 additional veterinarians were recruited on a permanent basis in June 2002. Furthermore, 5 veterinarians and 20 veterinary inspectors have been recruited on a temporary basis as from April 2002. As regards the State General Laboratory, 11 out of 18 laboratories were accredited in March 2002.

In the field of **phytosanitary issues** good progress has been made, with the adoption of a large volume of implementing legislation in April and September 2002 respectively, such as the Plant Propagating Material Law, the relevant Plant Propagating Material Regulations, the Seed Law and five relevant Seed Regulations. The Pesticides Authorisation board decided not to authorise in the future any substances that are not already authorised in at least one Member State. Two active substances currently authorised in Cyprus are not authorised in Member States and their use will be prohibited upon accession.

As regards **food safety** (*see also chapter 1 - Free movement of goods*), there has been some streamlining of the institutions responsible for inspections related to food safety, since in November 2001 the Veterinary and Food Board took over the control of non-animal food production and wholesale from the National Health Inspectorate. Co-operation between the Veterinary and Food Board, the Plant Protection Inspectorate, the Ministry of Agriculture and the Customs Board seems to be working well, with an inter-institutional agreement between the Customs Board, the Veterinary and Food Board and the Plant Protection Inspectorate having been concluded in April this year.

The upgrading of food processing establishments has been progressing well particularly in the meat sector, though the dairy sector is less advanced. Cyprus has established a detailed action plan to tackle this problem and all establishments have produced an upgrading plan in order to be in compliance by the date of accession.

BSE testing measures are being implemented and these are now almost at the same level as in the EU, having been increased considerably since the previous report. Further work is required to meet EC standards regarding animal waste processing, and plans to build a new central processing facility are progressing well.

Regular surveillance continued for the potato nematode, citrus nematode and banana nematode. The results are computerised and entered on aerial maps indicating the degree of infestation. The surveillance programme is also implemented for the citrus tristeza virus. Monitoring programmes also exist for other pests and diseases to facilitate IPM programmes.

Overall assessment

Concerning **horizontal issues**, priority should be given to further development of the Paying Agency and especially to the preparation of IACS (particularly the land parcel

identification system, LPIS). A basic IACS unit has been formed in the Department of Agriculture to promote and follow up the preparatory work. Further enhancement and strengthening of the unit is necessary. Planning to have LPIS in place by accession is progressing. However, for a functional LPIS much depends on the effectiveness of the cadastre data, and it is important that the present rhythm of preparations is maintained. Bearing in mind the proposed timetable for the implementation of the IACS software and hardware, and taking into account the need for testing and training, considerable efforts are still required to finalise preparations by the time of accession.

In the field of *quality policy* the new Quality Control of Agricultural Products Law aims at aligning with the *acquis*.

As regards *organic farming*, the adoption of the national law and its relevant regulations on Organic Farming have been an important step forward in aligning Cyprus legislation with the *acquis*, particularly in terms of control. The Department of Agriculture, MANRE, will have the main responsibility for implementing the *acquis* in this field. It's basic tasks will be the setting up of the inspection system, to implement related administrative tasks, to take the general enforcement measures and to exchange information required by the relevant EC Regulation. The procedure for the recruitment of 30 new officers for the Department is ongoing.

As regards **common market organisations**, Cyprus has continued its alignment with the *acquis* by preparing the abolition of the Cyprus Grain Commission and by implementing an area-based payment for cereals, fodder crops and grain legumes. For the fruits and vegetables sector, the administrative capacity is in place. For olive oil, Cyprus should have an olive oil registry in place in 2002 but will need to make further efforts in order to have a GIS by accession, to comply with the requirements with the *acquis*. For milk and dairy products, Cyprus should have no problem in managing the CMO, as a quota system, an export refund scheme and a private storage scheme are already operational. Regarding the meat sector, Cyprus will have more than one year to implement the carcass classification system and the reporting of prices, which should be enough time to train the staff in charge of the classification.

With regard to **rural development**, Cyprus has started to design its rural development programme, and no major problems are expected in this field.

Concerning the **veterinary field**, the four remaining framework laws that provide the legal frameworks for the transposition of the veterinary *acquis* still need to be enacted.

Currently there are no complete lists of third countries or lists of establishments from which exports are allowed to Cyprus. Import licenses are issued on the basis of the sanitary situation in the exporting countries, but there are no clear criteria in place for this. The Ministry of Agriculture (Veterinary services) and Ministry of Health services share the competencies for import controls. The new legislation, concerning the import procedures, states, that these competencies would be assigned to the veterinary services except for the labelling and additives that will remain under the Ministry of Health supervision. The office, laboratory equipment and other facilities at the Border Inspection Posts (BIP's) need to be upgraded. Training of the staff needs to be enforced. Two BIPs are foreseen in Cyprus, at Limassol port and Larnaka airport. There are some facilities in place in Larnaka but further modifications are to be made before the border inspection post is fully completed to EC requirements. For Limassol port no facilities are yet in

place. Given the limited progress so far especially with regard to Limassol very serious efforts are required to ensure that the deadlines set for completion can be met, so that the posts can be ready by accession. As regards staff, more needs to be done to familiarise them with EC procedures.

In the **phytosanitary field** the legal vetting of the new phytosanitary framework law, should be finished soon and enactment is planned by the end of 2002. Revised legislation to the Pest Control Products Law and the corresponding regulations has been drafted and needs to be approved. The framework law on plant quarantine has not been adopted so far, which is a cause of serious concern.

The Agricultural Research Institute will be acting as the testing station for tests needed for plant variety registration.

As regards **food safety** (*see also chapter 1 - Free movement of goods*), as is mentioned above, considerable progress has been made, particularly regarding the upgrading of food establishments and the increase in measures to deal with BSE.

The reorganisation of some of the bodies dealing with food safety i.e. the national food laboratory and the plant hygiene laboratory, in line with the Food Safety Strategy should further improve effectiveness in this area.

Conclusion

In its 1998 Regular Report, the Commission concluded that, in recent years, Cyprus has progressed in preparing the integration of its agriculture and agricultural policies into the Common Agricultural Policy. This process needs to be continued. Given the small size of the Cypriot agricultural sector, Cyprus's accession should not have any major impact on Community markets.

Since the 1998 Regular Report Cyprus has made considerable progress toward alignment with the EC agricultural *acquis*. In terms of preparations to apply the Common Agricultural Policy, significant steps have been taken, particularly the adoption of primary and implementation legislation. However, market intervention systems in line with the *acquis* are not yet fully established. Producers still face problems in marketing their products, although these may be partly alleviated through a better structure of producer co-operatives, which will be encouraged through the support schemes for producer organisations currently being launched and developed. The alignment with the *acquis* is at an advanced stage. Cyprus has reached an adequate administrative capacity to implement the *acquis*.

Negotiations on this chapter continue, although all negotiation issues in the veterinary and phytosanitary fields have been clarified. Cyprus has been granted a transitional arrangement in relation to the quality requirements for certified and local seeds (for a period of five years as of the date of accession), and a technical request to the effect that provisions for placing on the market of dogs and cats in the UK apply to Cyprus. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on finalising alignment, further reinforcing the administrative capacity to implement and

enforce the *acquis*, in particular in the veterinary field and that of food safety, ensuring that establishments are duly upgraded to meet Community Standards and concluding the process of agricultural land reform. Due priority should be given to the preparation of the Integrated Administration and Control System, in particular the development of the land parcel identification system.

Chapter 8: Fisheries

Progress since the last Regular Report

Since the last Regular Report, Cyprus has made further progress, notably in the field of resource management, inspection and control, while the administrative capacity has been strengthened.

As regards **resource management, inspection and control**, the Inspectorate Service of the Department of Fisheries and Marine Research has appointed an additional inspector, bringing the total number of inspectors to 15.

The Fisheries Department has revised its initial plans for the acquisition of a multi-purpose patrol vessel, and has decided that such a vessel is not a high priority, at least for the time being.

In the field of **structural actions**, Cyprus continues its efforts to reduce the number of fishing vessels under its flag that operate in the high seas. It has reduced the number of fishing vessels above 24 metres from 104 in 1999 to about 30 today, thereby gradually reaching its target to reduce the number to 20 by accession. The establishment of a Fishing Vessel Register, in line with the requirements of the *acquis*, is being pursued. The relevant hardware and software have been installed.

As regards **market policy**, a law on the recognition of producers' organisations and aquaculture products has been enacted.

Concerning **state aid to the fisheries sector**, no particular developments are to be reported.

As regards **international fisheries agreements**, three fisheries agreements and one convention have been ratified by the House of Representatives. They concern the 1993 FAO Agreement to promote compliance with International Conservation and Management Measures by Fishing Vessels on the High Seas, the 1995 UN Agreement for the Conservation and Management of Straddling Fish Stocks and highly Migratory Fish Stocks, the International Convention for the Conservation of Atlantic Tunas and the amendments to the General Fisheries Commission for the Mediterranean. Furthermore, the Protocol on the Association Agreement between the European Community and the Republic of Cyprus for the determination of the Trade Arrangements for certain Fish and Fish Products has been ratified in September 2002.

Overall assessment

As regards resource management, inspection and control, the equipment of the Department of Fisheries and Marine Research still needs to be improved. The number of

inspectors in the Inspectorate Service of the Department of Fisheries and Marine Research is to reach 20 by 2003 which seems to be appropriate in relation to the size of the fleet.

The satellite monitoring system for the control of vessels fishing in the high seas, which Cyprus decided to implement itself, is to be established at the end of 2002. It has been decided that the vessel monitoring system (VMS) will be installed at the Department of Fisheries and for this purpose new premises have to be rented.

As regards market policy, no further alignment is required at this stage following the adoption of the law on the recognition of producers' organisations.

A set of regulatory acts relevant to the new law for aquaculture still needs to be enacted.

As regards structural measures, the Fishing Vessel Register, which Cyprus had planned to introduce by the end of 2001, still has to become fully operational. Preliminary work on the drafting of the Single Programming Document for fisheries measures to be part-financed under the Community Financial Instrument for Fisheries Guidance (FIFG) was initiated. Cyprus's policy of reducing the number of fishing vessels sailing under its flag that operate in distant waters is continuing at a steady pace.

Conclusion

In its 1998 Regular Report, the Commission concluded that the alignment of legislation and administrative reforms in Cyprus should not pose major problems. However, reforms in the administrative structure had not been undertaken nor legislation adopted, in particular concerning fleet register, control policy and norms of commercialisation in order to ensure the implementation of the Common Fishery Policy. Control mechanisms on inspection facilities and infrastructure in the Department of Fisheries would have to be strengthened.

Since the 1998 Regular Report, Cyprus has progressed, notably in the area of administrative structures and in adopting legislation, including the fleet register. Cyprus has reached a reasonable level of legislative alignment. The administrative capacity is in place but needs further reinforcement.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. Cyprus is meeting the majority of the commitments it has made in the accession negotiations in this field. However, delays have occurred in adopting legislation on structural actions and on the establishment of the Fishing Vessel Register. These issues must be addressed.

In order to complete preparations for membership, Cyprus's efforts now need to focus on the adoption of the outstanding legislation, as well as on further reinforcing its capacity for implementation and enforcement.

Chapter 9: Transport policy

Progress since the last Regular Report

During the past year, Cyprus has continued to align its legislation with the *acquis* and made progress, particularly in the field of road and maritime transport, as well as strengthening administrative capacity in those sectors.

As regards **Trans-European Transport Networks**, no particular legislative developments are to be reported.

In the **land transport** sector, progress has been achieved, especially in the field of technology and safety legislation, also through the adoption of secondary legislation. In March 2002 a number of regulations were approved that provide for the installation of tachographs in newly registered vehicles, as well as in existing buses and heavy goods vehicles engaged in international transport. A law on Vehicle Taxes was enacted in March 2002, completing harmonisation with the fiscal *acquis* on charging for heavy goods vehicles. Subsequently the Motor Vehicles (Drivers' Hours of Work) Law and the Road Transport Law were enacted by the House of Representatives in June and July 2002 respectively.

New legislation on an accounting system for expenditure in respect of transport by rail, road and inland waterways was enacted in November 2001.

A law and regulations concerning the minimum training level for professional road transport drivers were enacted in November 2001. Since January 2002, all new cars must have safety belts on all seats and as from July 2002, all cars registered after January 1998 must have safety belts on all seats. Furthermore, the use of safety belts became compulsory for all passengers.

Since October 2001 technical inspections of private vehicles have been carried out by over 70 private testing centres, which are supervised by the Department of Road Transport. Roadworthiness tests for public service vehicles, trailers and high-risk vehicles are carried out by the Technical Services Division of the Department of Road Transport on a regular basis at four testing stations. The Department of Road Transport Inspectorate will be reorganised in order to enable it to perform its supervisory and control functions. A staff increase of 48 additional experts has been approved for 2002, and further increases are planned for 2003.

Amendments of the Law on the Admission to the Occupation of Road Haulage Operator and its relevant regulations, and the Road Transport Regulations have been approved by the House of Representatives in September 2002. The AETR Agreement has been ratified.

In the field of **air transport**, regulations on air traffic management equipment and systems for the adoption of EUROCONTROL standards entered into force in February 2002. A law was passed in March 2002 ratifying the Montreal Convention for the Unification of Certain Rules for International Carriage by Air.

A study of the capacity of Larnaca and Paphos airports has been completed.

In the field of **maritime transport**, Cyprus made progress with legislative alignment in May 2002 by transposing legislation on marine equipment, on setting up a harmonised safety regime for fishing vessels of 24 metres in length and over, on the registration of persons sailing on board passenger ships operating to or from ports of the Member States of the Community, on safety rules and standards for passenger ships and on a system of mandatory surveys for the safe operation of regular ro-ro ferry and high speed passenger craft services. In June 2002 the Merchant Shipping Law was enacted.

With regard to the effective implementation of the International Safety Management (ISM) Code, during the first five months of 2002, the Cyprus Authorities revoked the Documents of Compliance of 3 companies managing 4 Cyprus flag vessels in total. One of these Documents of Compliance has been reinstated as a result of successful additional audits on shore and on board the vessels. With regard to flag State control, the number of inspections carried out by the Department of Merchant Shipping (DMS) Marine Surveyors and through the global network of Flag State Inspectors has increased significantly during the last four years. They carried out 593 inspections in 2001, as compared to 527 in 2000, 369 in 1999 and 166 in 1998.

According to 2001 statistics under the Paris Memorandum of Understanding (MoU), the percentage of Cyprus flag vessels detained following Port State control was 8.85%, a further decrease compared with 2000 (9.71%) and 1999 (9.97%). This compares with an average for EU-flagged vessels of 3.14% in 2001.

The Department of Merchant Shipping (DMS) in September 2001 started issuing recognition endorsements to all officers serving on board Cyprus ships and Seafarer's Identification and Sea Service Record Books to all seafarers serving on board Cyprus ships. As from November 2001, the Government of the Republic requires all seafarers serving on board Cyprus ships to be registered in the Cyprus's Seafarer's Register and to hold valid Cyprus Seafarer's Identification and Sea Service Record Books.

As regards *administrative capacity* the global network of ship inspectors has been strengthened with the appointment of additional ship inspectors at various ports, thus bringing the total of ship inspectors world-wide to 35. In an effort to co-ordinate their approach with the recognised classification societies and to further enhance the control of Cyprus ships, the Department of Merchant Shipping has held consultative meetings with the International Association of Classification Societies (IACS). Within the framework of the Action Plan, 25 new posts for professional and clerical staff have been created for the Department of Merchant Shipping (11 Marine Surveyors, 4 Merchant Shipping Officers and 10 Clerks/Merchant Shipping Assistants).

Overall assessment

As regards *land transport*, the Cyprus legislative framework has reached a fair level of alignment with the *acquis*, except for alignment with the *acquis* on transport of dangerous goods. Cyprus has also to address the issue of ensuring that current road transport operators meet the *acquis* in terms of admission to the occupation. The implementing capacity of the Departments involved has to be gradually reinforced so that they will be in a position to implement the transport *acquis* by January 2003. It will be necessary to set up a new system for enforcing the legislation on driving and rest periods, in compliance with the requirements for inspection, and to set up a new unit within the Department of Road Transport to deal with market access issues. The Road Transport

Control Division of the Department of Road Transport needs to be further enhanced. As regards Trans-European Networks, special emphasis should be given to ensure the necessary administrative capacity (both in qualitative and quantitative terms) to prepare for the significant investments that will be needed in transport infrastructure.

On *air transport*, there are still outstanding discrepancies with the *acquis*. Compliance with the relevant *acquis* should be achieved through the adoption of the new Civil Aviation Bill by the end of 2002. An independent Air Accident Investigation body still has to be established. Also the effective capacity of the Department of Civil Aviation has to be further enhanced through implementation of the action plan on “Development of Safety Oversight Capabilities” in order to align with EU rules on aircraft maintenance standards and flight operations inspections.

On *maritime transport*, Cyprus has made progress in terms of legislative transposition, and alignment with the applicable *acquis* is practically completed. Further transposition is needed with regard to the *acquis* on seafarers' hours of work and on port reception facilities for ship-generated waste and cargo residues. Cyprus has also made substantial progress in terms of reinforcement of the administrative capacity of the Department of Merchant Shipping and improving safety standards through tighter controls. However, in these last two fields, efforts should be sustained to meet the staffing target in order to ensure that Cyprus will meet its objective of removing the Cypriot flag from the Paris MoU black list. Also full computerisation of the Department of Merchant Shipping through the implementation of the “MARCOS” system needs to be completed.

Conclusion

In its 1998 Regular Report, the Commission concluded, that efforts on maritime safety were very limited. Outstanding transpositions raised particular concern due to the size of the fleet, the lack of enforcement of standards and the subsequently persisting high detention rates. Progress had been achieved in the fields of air and road transport, though further efforts would be necessary. Enforcement capacities needed further monitoring.

Since the 1998 Regular Report, Cyprus has made steady progress in aligning its legislation, except in the air transport sector. Laws in the transport sector are now to a great extent in line with the *acquis*, the relevant framework laws are in place and only a limited amount of secondary legislation remains to be transposed. Cyprus has also gradually reinforced its administrative structures, but need further strengthening.

Negotiations on this chapter have been provisionally closed. Cyprus has been granted a transitional arrangement as regards recording equipment for existing vehicles engaged in national transport (until 31 December 2005). Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on the completion of alignment and implementation of maritime transport legislation, in particular enforcement of maritime safety standards, continued alignment in road transport, notably transport of dangerous goods and air transport.

Chapter 10: Taxation

Progress since the last Regular Report

Since the last Regular Report, Cyprus has made significant progress in aligning its tax legislation with the *acquis*, especially through the adoption in July 2002 by the House of Representatives of a comprehensive tax reform, concerning both indirect and direct taxation.

Concerning **indirect taxation**, the VAT rate was increased from 10% to 13% from July 2002 and it will be further increased to 15% as from January 2003 as a part of the tax reform.

The new Value Added Tax (VAT) Law of 2000 and relevant regulations came into force in February 2002. This provides *inter alia* for the elimination of the special VAT regime in favour of international business enterprises, as well as for a VAT refund scheme for foreign taxable persons not established within Cyprus.

As concerns excise duties, in December 2001 the excise duty on imported beer was increased, and in May 2002 the excise duty on cigarettes was increased. As concerns import duties, some measures were taken, stopping short of abolishing them. In particular, the import duties on beer imported from the EU and on spirits of an alcoholic strength not exceeding 10% volume were reduced.

The significant tax advantage applied to twin cabin and Jeep-Type 4x4 motor vehicles as opposed to saloon cars was reduced in July 2002.

In the field of **direct taxation**, legislation aiming at simplifying the tax system and harmonising with the *acquis* (Income Tax Law, Special Contribution for the Defence Law, Capital Gains Tax Law, Stamp Duty law, and the Assessment and Collection of Taxes Law) was enacted in July 2002. The tax reform abolished the current preferential tax scheme for International Business Enterprises by way of introducing a unified tax rate of 10% for both domestic and foreign companies by January 2003.

As regards **administrative co-operation and mutual assistance**, no particular developments are to be reported.

As regards *administrative capacity*, the project to upgrade and update the existing computerised VAT system to comply with the new VAT Law has been completed. In the area of direct taxation, the Department of Inland Revenue was strengthened with the employment of 40 additional income tax officers in the year 2001.

Overall assessment

The main challenge in the field of excise duties relates to alignment with the Community's minimum excise duty levels on most of the harmonised excise duty product categories (alcoholic beverages and mineral oils) and the complete elimination of existing protective import duties, so as to ensure equal taxation irrespective of origin. Further action is also required for the establishment of the required tax warehouses for excisable products.

As regards *direct taxation*, the legislation will have to be reviewed in order to eliminate potentially harmful tax measures, so as to comply with the Code of Conduct for Business Taxation to the same extent as current Member States upon accession. The Commission's initial technical assessment of potentially harmful measures applied in Cyprus is ongoing. The modernisation of the tax administration so as to reinforce its capacity for implementation and enforcement of the *acquis* is still in its preparatory phase. The preparations are progressing according to plans. Following the successful implementation of the national system for VAT Information Exchange, electronic submission and processing of tax returns and other measures currently in progress, Cyprus's level of Information Technology is expected to be satisfactory upon its accession to the EU.

Conclusion

In its 1998 Regular Report, the Commission concluded that, although alignment of VAT law with that of the European Community had taken place, further progress remained necessary, in particular as regards the application of VAT rates (scope and rate levels), a refund scheme for foreign taxable persons not established in Cyprus and the taxation of farmers. Furthermore, Cyprus was recommended to initiate preparations for the European Community's transitional VAT regime and to strengthen arrangements for administrative co-operation and mutual assistance, as well as the administrative capacity for implementation. In the field of excise some essential problems remained which would require significant efforts in order to align Cyprus's excise legislation to that of the European Community.

Since the 1998 Regular Report, Cyprus has made significant progress in aligning with the *acquis* on indirect and direct taxation. Cyprus has also made important progress with developing the necessary administrative capacity to implement and enforce the *acquis* in this area. While the implementation of the new VAT Act and the adoption of the tax reform has moved Cyprus significantly forward, alignment still needs to be completed as regards the special flat-rate scheme for farmers, the special scheme for investment gold, the taxation of immovable property and intra-Community transactions. Overall, alignment of legislation has reached a good level. The administrative capacity to implement the *acquis* in this area has reached an adequate level.

Negotiations on this chapter have been provisionally closed. Cyprus has been granted for an indefinite period of time the right to apply a VAT registration and exemption threshold of € 15,600 for small and medium-sized enterprises. Furthermore, Cyprus has been granted transitional arrangements concerning the application of the VAT-zero rate on supplies of foodstuffs for human consumption and pharmaceuticals (until 31 December 2007), the application of the reduced rate of 5% on restaurant services (until 31 December 2007), maintaining the exemption on the supply of building land (until 31 December 2007), the application of an exemption from excise duties for mineral oils used for the production of cement (for a period of one year following accession) and reduced excise duties rates for all types of fuel used by local passenger transport vehicles (for a period of one year following accession). Furthermore, Cyprus has been granted a specific arrangement for simplified VAT procedures regarding the application of a cash accounting scheme and for the values of supplies between connected persons (for a period of one year following accession). Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts should now focus on completing transposition - except for areas where transitional arrangements have been agreed – in the area of VAT - and excise duties, including intra-Community transactions. Cyprus should also further pursue the measures taken to modernise and reinforce the tax administration.

Chapter 11: Economic and Monetary Union

Progress since the last Regular Report

A detailed assessment of the various aspects of Cyprus's economic policy has been given above, in the chapter discussing the economic criteria (B-2). Therefore, the present section is limited to a discussion of those aspects of the Economic and Monetary Union *acquis* – as defined by Title VII of the EC Treaty and the other relevant texts – which candidate countries should implement before accession, i.e. the prohibition of direct public sector financing by the central bank, the prohibition of privileged access of the public sector to financial institutions, and the independence of the national central bank. As to the process of liberalisation of capital movements, upon the completion of which compliance with the EMU *acquis* is conditional, this aspect has been covered above (*see Chapter 4 – Free movement of capital*).

Since the last Regular Report, Cyprus has made significant progress in the adoption of EMU-related *acquis*.

As regards the **prohibition of direct public sector financing by the Central Bank**, The Central Bank of Cyprus Law of 2002 as well as the amendments of the pertinent Constitutional provisions entered into force in July 2002. The act includes an explicit prohibition of direct financing of the public sector by the Central Bank. Furthermore, it provides that the stock of outstanding claims of the Central Bank on the public sector, comprising direct advances, treasury bills and government and government-guaranteed securities will be converted into a loan with a maturity of 30 years and an interest rate of 3%. The new act has also largely aligned Cyprus's legislation with the *acquis* in the area of **central bank independence**.

As regards the prohibition of privileged access of the public sector to financial institutions, no developments have been recorded since the last Regular Report.

Overall assessment

Cyprus will participate in EMU upon accession with the status of a country with a derogation under Article 122 of the EC Treaty, and it will need to implement the necessary changes to its institutional and legal framework by the date of accession.

The legislative implementation of the *acquis* has been broadly completed with the entry into force of the Central Bank of Cyprus Law. In terms of the prohibition of privileged access of the public sector to financial institutions, there are no regulations that have been identified which would be incompatible with the *acquis*.

Conclusion

In its 1998 Regular Report, the Commission concluded that Cyprus continued to prepare for integration into Economic and Monetary Union, but it stressed that the Central Bank of Cyprus was not independent from the Government and that Cyprus did not comply with the Treaty on the issue of Central Bank financing, although a ceiling for such financing had been set in 1994. Also, no information was available on the issue of the privileged access of the Government to financial institutions. The Commission also pointed out that, upon accession, Cyprus would be required to renounce any direct central bank financing of the public sector deficit and privileged access of public authorities to

Since the 1998 Regular Report, Cyprus has made significant progress. The alignment with the *acquis* is at an advanced stage. Administrative structures are in place.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts should focus on strengthening the administrative capacity of the Central Bank of Cyprus.

Chapter 12: Statistics

Progress since the last Regular Report

Cyprus has continued to make good progress over the past year.

In the field of **statistical infrastructure**, the Cypriot Statistical Office (CYSTAT) has succeeded in increasing its human and financial resources so as to meet the requirements of harmonisation. Additional staff were recruited on a temporary and permanent basis.

As regards **classifications**, Eurostat has approved the Cypriot proposal for the Nomenclature of Territorial Units for Statistics (NUTS) for Cyprus. Major economic classifications are in place.

As regards **demographic and social statistics**, the Census of Population was carried out in October 2001 in accordance with the UN/ECE/Eurostat recommendation and preliminary results were published in January 2002. For the first time, the ad hoc module on employment of disabled people has been included in the labour force survey.

In the area of **macro-economic statistics**, Cyprus has adopted as from January 2002 the fully harmonised indices of consumer prices. Cyprus is carrying out a full programme of price surveys with a view to establishing purchasing power parities. A new Balance of Payments data collection and compilation is being implemented as from January 2002. A regular reporting system on foreign direct investments (FDI) statistics has been set up by the Central Bank of Cyprus in accordance with the ECB's requirements. The necessary framework for compiling quarterly national accounts has been set up.

In the area of **business statistics**, no particular developments are to be reported. As regards **transport statistics**, a new survey on transport of goods by road has been

introduced as from January 2002, which is in line with the EC regulation. The Cyprus Ports Authority has implemented the survey of goods and passenger transport by sea.

The Cyprus Tourism Organisation has introduced a new system for the collection of harmonised statistics on "guest flows", "guest nights" and occupancy from collective accommodation establishments in line with the *acquis*. The survey on passengers carried out at the point of arrival and the survey on long-term and short-term migrants have been expanded, according to the revised recommendations on international migration. Also a new border survey at the points of departure has been introduced.

As for **external trade**, preparatory work for the introduction of INTRASTAT, which measures the internal trade among Member States, has commenced in co-operation with the VAT Service.

In **agricultural statistics**, preparation of the 2003 census is ongoing.

Overall assessment

The fundamental principles of impartiality and reliability of data, transparency of statistics and confidentiality of personal data are safeguarded. Furthermore, CYSTAT maintains full independence and autonomy in methodological matters, techniques and procedures for producing and disseminating data. Cyprus has made efforts to ensure that adequate human and financial resources are allocated to further strengthen statistical capacities, including at regional level, as there is an urgent need for more staff.

Conclusion

In its 1998 Regular Report, the Commission concluded that Cyprus still had some way to go to meet the requirements of the European system.

Since then, Cyprus has made considerable progress in adopting the *acquis*, in particular with the enactment of the new Statistical Law in February 2000, which takes account of the relevant statistical *acquis* and is based on a detailed programme of harmonisation prepared already in 1998. Cyprus has the basic infrastructure for meeting the EC requirements in the field of statistics and no further legal transposition is required.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in statistics and is generally meeting the commitments it made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on enhancing the implementation of the European System of Accounts (ESA 95) methodology and the full functioning of the INTRASTAT mechanism.

Chapter 13: Social policy and employment

Progress since the last Regular Report

Substantial progress has been made in this area since the last Regular Report.

As regards **labour law**, legislation has been enacted with the aim of transposing the Directives on the posting of workers, working time, part-time work, the safety and health of workers with a fixed-duration or temporary employment relationship and the European Works Council. An Independent Fund has been set up based on the provisions of the Insolvency Directive.

Concerning **equal treatment for women and men**, legislation was adopted in May 2002 for the transposition and implementation of the *acquis* regarding health and safety of pregnant workers and parental leave. The law on Equal Treatment for Men and Women in Occupational Social Security Schemes as well as the Provision Fund Law was enacted in July 2002. The law restricting women from working during the night was repealed in July 2002. The law on equal pay for men and women for work of equal value was enacted in September 2002.

In the area of **health and safety** at work, substantial progress was made during the reporting period with the transposition of the *acquis* in the fields of the management of safety and health at work, the minimum safety and health requirements for workplaces and for work on board Cyprus-flagged fishing vessels, the use of work equipment, the use of personal protective equipment, work with display screen equipment, temporary or mobile construction sites, protection from risks related to exposure to noise at work and the safety of workers in the mineral-extracting industries and in potentially explosive atmospheres.

Concerning **public health**, the transposition of the tobacco legislation progressed in May 2002 with the adjustment of the tar yield to the required level and a new laboratory for measuring the tar yield of cigarettes was created at the General State Laboratory of the Ministry of Health.

With regard to **social dialogue**, social partners participated in the preparation of all legislative measures, ensuring that all parties expressed their views. They were also informed about every part of the *acquis* that had been adopted and so were given the chance to inform their members, well in advance, about the new environment to which they have to adjust.

As regards **employment policy**, the Joint Assessment of Employment Policy Priorities (JAP) was signed by the Commission and the Cypriot Government in December 2001. As part of the monitoring process of the Employment Policy Review, a progress report on the implementation of the priorities identified in the JAP was submitted to the Commission by Cyprus in June 2002. This report presents an important step in assessing the extent to which Cyprus is progressing towards its objectives of labour market reform and adaptation of its employment system in order to prepare for future participation in the European Employment Strategy after accession. The labour market performance remains strong with the rate of unemployment in Cyprus further declining from 4.9% in 2000 to 4% in 2001. Female unemployment is still higher than male unemployment (5.8% and 2.7% respectively).

Concerning the preparation for the European Social Fund (ESF), the Planning Bureau has been designated as the Single Managing Authority for the Structural Funds.

As a follow-up to the Gothenburg European Council, where the EU invited the candidate countries to translate the EU objectives into their national policies, the Commission and Cyprus have initiated a joint co-operation exercise to prepare for future participation in

the EU **social inclusion** process after accession. This exercise consists in joint identification of the social exclusion challenges and relevant policy responses.. In this context, the Statistical Office of Cyprus co-operates with Eurostat to produce data on poverty and social exclusion.

As regards other areas of **social protection**, a law for Child Benefit for Families with three children has been enacted and the law amending the Public Assistance and Services Law has been approved. In July 2002, the Council of Ministers approved the signing of the European Convention on the exercise of Children's Rights.

No progress can be reported with regard to the transposition of the Community *acquis* in the field of **anti-discrimination** (*see also Section B.1.2 - Human rights and the protection of minorities*).

Concerning *administrative capacity*, the Ministry of Labour and Social Insurance commissioned a human resources needs assessment, and identified urgent short-term and long-term needs for the increase in permanent staff. The original estimate amounted to an additional 150 officials for the Ministry. In the meantime, a supplementary budget is before the House of Representatives to request 41 additional staff as an urgent measure in the run-up to accession. A further needs assessment will be undertaken at a later stage to verify whether an additional increase in staffing is necessary.

Overall assessment

In the area of labour law, the majority of the *acquis* has been transposed. The legislation transposing the Directives on the European Works Council and on posting of workers will enter into force upon accession. Cyprus will also have to transpose the Directives related to the involvement of workers in the European Company and to the information and consultation of workers.

With regard to the equal treatment for women and men, the new law transposes the *acquis* on equal pay. In the field of health and safety at work important progress has been made and alignment is almost complete even if some regulations transposing the *acquis* will only enter into force in 2003. Follow-up for the effective implementation of these regulations is needed.

With regard to public health, the updated tobacco *acquis* needs to be implemented. Both the network for the surveillance of communicable diseases and the health monitoring system are under preparation. To improve the enforcement of EC legislation in the area of communicable disease control and surveillance, the following actions are recommended: quick implementation of the new surveillance system, establishment of a public health laboratory network based on designated reference centres, collaboration with EC specific disease surveillance networks and organisation of training in field epidemiology. For the prevention of AIDS and communicable diseases, the creation of a Public Health Laboratory is planned. A medical officer has been designated to develop a Health Monitoring System and training has been assured to implement the Health Care Information System to be installed at the New Nicosia Hospital.

Social dialogue is well-established in Cyprus. The social partners played an active role in the preparation of legislative measures for the transposition of the *acquis*. Autonomous bipartite social dialogue between employer and worker representatives must be strengthened, including at sectoral level.

Regarding employment, the Joint Assessment of the Employment Policy Priorities for Cyprus (JAP), represents an important step in the preparations for accession. Progress in the implementation of these policies is assessed regularly and it will be important to ensure effective monitoring of the phasing-in of the priorities and commitments contained in the JAP. Employment policies should aim at increasing the overall employment rate, in particular for women, address the emerging skill mismatches and skill shortages and increase the incentives for inactive and unemployed people to active job search and take up jobs. It will be important to reform the vocational and education system, to address skill shortages and to increase employment rates for women. Further efforts are required to modernise the PES to meet the needs of employers and jobseekers, in particular the IT systems related to job-brokering.

There is a strong need for enhancing administrative capacity. Immediate action is called for to strengthen the Ministry of Labour and Social Insurance in view of the implementation of the legislation in the field of safety and health, labour law, gender equality and anti-discrimination as well as the preparation for the management of the ESF.

A national integrated strategy on promoting social inclusion, taking into account the EU objectives, needs to be developed. As poverty and social exclusion is multidimensional by nature, it is important to promote an integrated approach mobilising various governmental bodies and all relevant stakeholders in the process. It is also crucial to improve and develop social statistics systems on poverty and social exclusion in line with the EU's commonly agreed indicators on social inclusion.

Legislation transposing the EC anti-discrimination Directives based on Article 13 of the EC Treaty will have to be introduced and implemented. Although the constitution of the Republic of Cyprus includes a general anti-discrimination clause, Cyprus must adopt specific legislation to transpose the *acquis*. Cyprus should also establish the Equality Body provided for in the *acquis*.

Conclusion

In its 1998 Regular Report, the Commission concluded that Cyprus had transposed part of the *acquis* in this chapter and that further progress was necessary, in particular as regards Labour Law and Occupational Health and Safety. The Commission added that Cyprus had effective enforcement structures.

Since 1998, Cyprus has made considerable progress, although uneven in the first two years. In a number of fields, legislative alignment has almost been completed. Some important measures still need to be enacted.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements. Cyprus is generally meeting the commitments it has made in the accession negotiations in this chapter.

In order to complete preparations for membership, Cyprus's efforts now need to focus on combat measures to discrimination and on the transposition and implementation of the relevant legislation. Administrative capacity needs to be strengthened through an increase in the number of staff.

Chapter 14: Energy

Progress since the last Regular Report

Cyprus has made limited progress in this field during the past year.

On the subject of **security of supply**, more particularly regarding oil stocks, no substantial progress was made.

As regards **competitiveness and the internal energy market**, the transparency of gas and electricity prices for the industrial end user law was approved by the House in November 2001. New legislation concerning crude oil supply costs and the consumer prices of petroleum products was approved in July 2002.

Concerning **energy efficiency and renewable energy**, a Law on efficiency requirements for certain categories of products was approved in March 2002, providing the basis for alignment with the energy efficiency *acquis*. An action plan submitted to the Council of Ministers provides, *inter alia*, for incentives for the promotion of photovoltaic, wind, solar, thermal, biogas and other energy resources. An amendment to the law on indication of consumption of energy and other resources of household has been enacted in September 2002.

As regards **nuclear energy**, Cyprus does not operate any nuclear power plant or other nuclear installation. Ionizing radiation is used in Cyprus, mainly for medical, but also for industrial, applications. Low-level sealed sources of both types are stored at the Nicosia General Hospital.

Cyprus has enacted the Framework Radiation Protection Law, which entered into force in July 2002. The Department of Labour Inspection at the Ministry of Labour and Social Insurance has been appointed as nuclear safety authority. The process of recruitment of new inspectors to the Department of Labour for the implementation of the legislation has started. Cyprus has established a Crisis Centre for all kinds of major disasters, including radiological emergencies.

Overall assessment

As regards security of supplies and oil stocks, Cyprus has advanced only in a limited manner. It needs to adopt the relevant legislation and to set up the oil stocks authority. Cyprus is also strongly encouraged to ensure the progressive building up of oil stocks according to the agreed timetable and as required by the *acquis*.

As regards competitiveness and the internal energy market, Cyprus has achieved only limited results. It needs to adopt the necessary legislation, which will provide for market opening in line with the Electricity Directive, the abolition of the monopoly status of the Electricity Authority of Cyprus (EAC), the establishment of an independent Regulator for electricity (and gas - even if, at present, gas is not used on the island) and a Transmission System Operator. Cyprus has to accelerate its efforts to set up the Regulator and to eliminate the remaining price distortions.

Cyprus has devoted efforts to improving energy efficiency and enhancing the use of renewable energy, but more needs to be done.

In June 2001, the Council of the European Union took note of a Report on Nuclear Safety in the Context of Enlargement. Although Cyprus does not generate electricity from nuclear power sources, the Report contains recommendations of relevance to Cyprus with regard to other nuclear installations, including the safe management of radioactive waste.

During the first half of 2002, a special Peer Review on nuclear safety assessed the progress made by candidate countries in implementing all the recommendations. This exercise, conducted under the auspices of the Council, resulted in a Status Report published in June 2002, which concludes that Cyprus has accepted and adequately addressed all the recommendations contained in the June 2001 Report on Nuclear Safety in the Context of Enlargement.

Cyprus will need to ensure compliance with European requirements and procedures. In this respect, due attention will need to be given to preparing the implementation of Euratom Safeguards, in particular regarding the reporting of nuclear material flows and inventories directly by the persons or undertakings operating nuclear installations or storing nuclear material. This includes small holders like universities, hospitals and medical practices. It should be noted that Cyprus has concluded a Full Scope Safeguards Agreement with the IAEA.

Conclusion

In its 1998 Regular Report, the Commission concluded that the vast majority of the *acquis* still needed to be transposed, although Cyprus had institutional structures and capacities to implement the *acquis* in this field. The Commission further noted the national regulatory energy objectives remained to be incorporated in the legal framework for energy and that special attention needed to be paid to the alignment and subsequent enforcement of the *acquis* on the Internal Energy Market, energy efficiency and oil stocks.

Since 1998, some progress has been made, especially concerning electricity and security of supply, at a moderate pace. Legislative alignment and implementation of the energy *acquis* is limited to date.

Negotiations on this chapter have been provisionally closed. Cyprus has been granted a transitional arrangement regarding the building up of oil stocks (until 31 December 2007). Cyprus is meeting the majority of the commitments it has made in the accession negotiations in this field. However, delays have occurred on the legal alignment as regards oil stocks and the alignment with the electricity Directive.

In order to be ready for membership, Cyprus's efforts now need to focus on adopting outstanding legislation and ensuring its full and timely application, in particular with regard to the internal energy market (electricity). Concerning oil stocks, Cyprus needs to make arrangements to ensure the finance to build up oil stocks and monitor the actual relocation of oil stocks sites. In addition, it needs to develop administrative capacities (energy regulator, oil stocks body). Preparatory work to design legislation in order to align with the internal energy market *acquis* is proceeding. As regards oil stocks, a draft bill establishing the oil stocks authority has been finalised. A decision has been taken on the site where storage capacity for oil stocks will be built. Negotiations regarding stockage of oil reserves on behalf of Cyprus by companies in Member States, for the

period of construction of storage capacity in Cyprus, are ongoing. These efforts should be continued without delay.

Chapter 15: Industrial policy²⁶

Progress since the last Regular Report

Since the 2001 Regular Report, Cyprus has made further progress in this field, particularly on the issue of the compatibility of its industrial policy schemes with state aid regulations.

The execution, monitoring and implementation of **industrial strategy** is the responsibility of the Ministry of Commerce, Industry and Tourism, which continued to implement satisfactorily the measures and incentives provided for in the New Industrial Policy. Co-operation with other Ministries and the Planning Bureau is well established.

The main objectives of Cyprus's New Industrial Policy are the provision of support for the restructuring of the country's traditional industries, the provision of assistance to existing production units and the attraction of high-tech industries and of capital-intensive foreign investment, the improvement of the environment of co-operation between enterprises, and the exploitation of industrial potential especially with regard to innovation and research and technological development.

All schemes referred to in Cyprus's New Industrial Policy were submitted for assessment to the Commissioner for State Aid in early 2002. Subsequently, some incentives/schemes were revised so as to achieve compliance with the state aid rules, and others are still under examination like the creation of business incubators and the scheme for the creation of new hi-tech enterprises through the business incubators. A contract has already been signed for the setting-up of the first incubator, whilst the target is to set up another three or four such incubators.

In the meantime, the Ministry of Commerce, Industry and Tourism has introduced certain additional schemes (such as for the enhancement of female entrepreneurship).

Investment promotion and foreign direct investment have been enhanced as a result of the recent measures to open the financial market and to reduce the relevant administrative procedures.

No new developments can be reported in the field of **privatisation and restructuring**.

The Government has decided to enhance the administrative capacity of the Ministry of Commerce, Industry and Tourism to ensure the effective implementation of the *acquis*.

Overall assessment

An important dimension of industrial policy is the control of state aid (*see also Chapter 6 – Competition policy*). Cyprus has made an important effort to make the schemes under

²⁶ Developments concerning Industrial policy should be seen in relation to the overall enterprise policy, including the SME policy (*see Chapter 16 - Small and medium-sized enterprises*).

its New Industrial Policy compatible with state aid rules. Nevertheless, it is important that such schemes should shift towards a more horizontal approach to boosting entrepreneurship and competitiveness rather than focusing on providing direct grants to companies.

With a view to accession, the Government is considering the preparation of a National Development Plan (2004-2006) comprising various projects that may be eligible for funding under the structural funds. Some of the schemes (mergers & acquisitions, sub-contracting) provide for the funding of studies for resolving management problems or other measures for SMEs, such as the adoption of the ISO 9000 quality management standard.

Conclusion

In its 1998 Regular Report the Commission reaffirmed, as stated in the Commission opinion of 1993 that integration into the European single market would not pose insurmountable difficulties for Cyprus, although many sectors still faced significant problems in restructuring.

Since the 1998 Regular Report, good progress has been made through reforms in the administrative structure and the adoption of legislation in order to ensure the competitiveness of Cypriot industry. Various actions have been carried out to improve productivity. The Strategic Development Plan for 1999-2003 focused on globalisation and trade liberalisation, technological changes and the information society. The industrial policy of Cyprus is generally in line with the concepts and principles of EC industrial policy.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this field. Cyprus is generally meeting the commitments it has made in the accession negotiations in this domain.

In order to complete preparations for membership, Cyprus's efforts now need to focus on fighting structural problems, such as high production costs and low productivity.

Chapter 16: Small and medium-sized enterprises²⁷

Progress since the last Regular Report

Cyprus has made some progress in this area since the last Regular Report.

As regards **SME policy**, in April 2002, Cyprus endorsed the principles of the European Charter for Small Enterprises as the basis for its action to support and develop small enterprises. The European Charter, adopted by the European Council in June 2000, is the reference document in the field of enterprise policy within the socio-economic strategy set up in Lisbon, that aims at creating in Europe the most advanced knowledge-based economy of the world by 2010. The reporting process on the implementation of the European Charter in Cyprus started in May 2002.

²⁷ Developments concerning SME policy should be seen in relation to overall enterprise policy, including industrial policy (*see Chapter 15 - Industrial policy*).

With reference to the **business environment**, a scheme providing government grants to promote entrepreneurship among women has been introduced and is in operation. Another similar scheme aiming at relocating small enterprises from residential areas was started in January 2002.

Many actions are carried out to develop entrepreneurial skills within enterprises. New schemes were introduced during the last year by the Human Resources Development Authority, such as a scheme on consultancy services for micro-enterprises and another on management for tertiary education graduates, while the Business Development Programme is being continued and reinforced.

Progress was made in the area of simplified rules for both new and existing enterprises. Company law and copyright legislation were recently streamlined.

The Government formulates and implements its policy for SMEs through the Ministry of Commerce, Industry and Tourism (MCIT) in consultation with private sector business associations. Its main objectives are the creation of a simplified legal and institutional framework for SMEs, the improvement of the financial environment and the enhancement of the competitiveness of SMEs through their internationalisation and access to the information society.

The Ministry of Industry promotes several schemes in the area of access to finance, such as a guarantee scheme, a grant scheme for technological upgrading, another for new and/or growing manufacturing companies in rural areas and a scheme to establish business incubators. These schemes to support SMEs in the manufacturing sector have been modified according to the provisions of the Public Aid Control Law.

Better access to new technology is a priority of the policy for SMEs in Cyprus. The Government signed the first contract for the setting up of a business incubator, whilst the target is to create a total of four.

A study to identify the problems facing SMEs in the retail sector and suggesting measures to improve its competitiveness and to identify areas where simplified procedures are urgent was completed and submitted to the Government.

Efforts should be strengthened to prepare for full use of the structural funds in the area of enterprise development.

No further progress can be reported as regards **SME definition**.

Overall assessment

In Cyprus there is a close cooperation of all the actors concerned, including the business community. Efforts are needed to increase entrepreneurial spirit among young people, in particular by including entrepreneurship in the education and training process through more developed links between enterprises and universities. Further improvements in administrative simplification for enterprises are still needed. The business community believes that access to finance for SMEs can be further improved. In this area, the liberalisation of the interest rates in 2001 and the consequent reduction of interest rates have improved the situation but there is still room for further improvements. On the banking side, interest rates and the collateral required could be further reduced, and on

the SME side, a less cautious attitude towards innovative sources of finance should be stimulated.

The SME definition is aligned with the EC Recommendation.

Conclusion

In its 1999 Regular Report, the Commission concluded that Cyprus's economy was dominated by SMEs, as only 36 enterprises could be classified as large companies based on the EU definition. It described the environment in Cyprus as conducive to private initiative.

Since 1999, Cyprus has improved the competitiveness of SMEs on the basis of the objectives set out in the Five Year Strategic Development Plan (1999-2003). Today Cyprus implements EU policies in this field and is generally in line with EU methodology and objectives.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. It is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on stimulating entrepreneurship in the education system. The process to facilitate the access to innovation for SMEs should be speeded up, in particular through the implementation of the planned business incubators. The level of expenditure for research and development should be increased.

Chapter 17: Science and research

Progress since the last Regular Report

During the period covered by this Report, Cyprus has made further progress in this field.

Cyprus continued to be fully associated with the Fifth **EC Framework Programme**. Cyprus expressed interest in being associated with the Sixth RTD Framework Programme (2002-2006).

Cyprus has recently increased its RTD spending in order to fill the gap with respect to EC average spending on R&D.

As part of this ongoing awareness-raising process, a number of briefing sessions focusing on the thematic and horizontal programmes of the Fifth Framework Programme have been organised by the Research Promotion Foundation in the past year.

Overall assessment

The authorities responsible for the formulation and implementation of the national science and research policy are the Planning Bureau and the Research Promotion Foundation. The Foundation is actively involved in the co-ordination and encouragement of the association of Cypriot institutions with the Fifth EC Framework Programme. A

national contact point system has been established as from 1999, which is co-ordinated by the Research Promotion Foundation.

Conclusion

In its 1998 Regular Report, the Commission concluded that the *acquis* in this field did not require transposition into national legislation.

Since 1998, progress has been made towards the promotion of science and research activities, the improvement of research infrastructure and the development of highly efficient mechanisms and administrative capacity. The framework for co-operation in the field of science and technology is well established. Cyprus has maintained its capacity to implement the *acquis* in this area.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts should continue to focus on measures needed to promote and enhance research and development, to further encourage research that supplies relevant technology to small and medium-sized enterprises, and to increase European co-operation in this field.

Chapter 18: Education and training

Progress since the last Regular Report

Cyprus has made further progress in this field since the previous report.

Regarding **Community programmes**, Cyprus continues to participate in the second generation of the Socrates, Leonardo da Vinci and Youth programmes (*see section A.b - Relations between the European Union and Cyprus*). In order to facilitate the European Voluntary Services Programme, which has been incorporated into the Youth Programme, amendments to the Insurance Company Law were approved.

As regards the **Directive concerning education of children of migrant workers**, the principles of existing legislation and practice are in line with the *acquis* and, in particular, provide for non-discrimination against children of foreign origin. There are already provisions in public schools for facilitating the reception of the children of migrants and teaching them the local language. A special teacher-training programme has been developed and is being carried out. The Ministry of Education and Culture also provides facilities for these children to learn their mother tongue and become aware of their cultural identity.

Cyprus has made progress in **reforming its education and training system**. Information technology was introduced in all primary schools and as a separate subject across the curriculum in all lower secondary schools (Gymnasia).

At the level of upper secondary school, a reform for secondary technical and vocational education was implemented in order to address, among other things, a series of key points in the Commission's Memorandum on Lifelong Learning such as: the increased emphasis

on core skills, autonomous learning, development of meta-cognitive skills, emphasis on learning mechanisms, integration of the use of information society technologies into vocational education and training, the upgrading of the curricula, and the training and retraining of teachers. Another major target of the revised technical and vocational education is to combine solid general education with new technological developments and the development of basic skills and abilities to face the challenges and needs of the labour market.

A major development relates to the decision of the Government to establish the Open University of Cyprus, so that equal opportunities are offered to all citizens by having access to university education, within the context of lifelong learning.

The Pilot Project for the development of standards for vocational qualifications has been completed for five key occupational areas.

Overall assessment

Necessary structures are in place to enable the implementation of the *acquis* and the participation in Community educational, vocational training and youth programmes. Participation in these programmes is satisfactory.

Conclusion

In its 1998 Regular Report, the Commission concluded that Cyprus's legislation had already incorporated the only act needing transposition, i.e. the Directive on the education of children of migrant workers. Although Cyprus had been participating in the Youth for Europe Community programmes in 1997-1999, Cyprus had to prepare the implementation of the EC youth policies and, in particular, the participation in the European Voluntary Service.

Since 1998, Cyprus has made continuous progress regarding the administrative framework and has proceeded with the carrying out of preparatory legislative measures in the fields covered by the *acquis* so that today the overall legal framework is in line with the *acquis*.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on the development and implementation of the reforms, including the development of a lifelong learning system, and of secondary technical and vocational education.

Chapter 19: Telecommunications and information technologies

Progress since the last Regular Report

During the period covered by this report, Cyprus made further progress in terms of adoption of a new regulatory framework and in the postal services.

There have been no new developments in the **liberalisation of the telecommunications market**. Penetration in mobile services has reached 46%. There is only one GSM operator and UMTS licences have yet to be issued. Fixed network penetration reached 63% and network modernisation is complete

As regards the **regulatory framework**, the Telecommunications and Postal Services Regulation Law of 2002 was adopted in March 2002 and the Radiocommunications Law in July 2002. However, as the Telecommunications and Postal Services Law will only come into effect after the adoption of the decrees for its application the *acquis* in this area will not be implemented before the beginning of 2003. Concerning the national regulatory authority (NRA), the Commissioner and Deputy Commissioner of Telecommunications and Postal Regulation took office in January 2002. Cyprus also appointed an Advisory Committee to advise the Commissioner on issues relating to the overall organisation and functioning of his office. To provide for the necessary staffing of the NRA, a regulation providing for the fast recruitment of personnel was adopted in June 2002. This allowed to start the recruitment of the 32 approved posts, of which 14 have already been hired.

In April 2002, the Government issued a public consultation paper on the introduction of competition in mobile telephony and in August 2002 it declared that a GSM licence for a second GSM network will be granted after an auction process in November 2002.

A new numbering plan has been prepared by the public network operator CYTA and came into effect in July 2002. The tariffs rebalancing scheme has been completed in April 2002, but cost-orientation of the tariffs is not yet achieved. In August 2002, the Commission for the Protection of Competition of Cyprus took action against CYTA for the abuse of its dominant position.

As from the introduction of eEurope+, the national action plan priorities, as well as the short- and medium-term measures, have been reviewed in order to accommodate the specific measures that have been adopted therein. The involvement of the private sector, including employers, SME organisations and trade unions, in redesigning policy measures was given particular attention.

Regarding **postal services**, the above-mentioned Telecommunications and Postal Services Regulation Law liberalised licensing and provided for universal service. With the appointment of the Commissioner of Telecommunications and Postal Regulation a proper regulatory body has been established in the field.

In addition, Cyprus prepared a five-year plan (2000-2006) for improving the quality of the services and with a view to introducing a management accounting system by the end of this year. The universal service has been further expanded to cover house-to-house delivery.

Overall assessment

Cyprus will need to transpose the updated telecommunications *acquis* before accession and to complete the implementation procedures as soon as possible afterwards

Although the Commissioner and the Advisory Committee for Telecommunications and Postal Regulation were appointed at the beginning of the year, progress in establishing

his office is slow because of the procedural requirements. As regards liberalisation, the provision of Internet services is the only market open to competition, in which CYTANET (a subsidiary of CYTA) still has a market share of about 50%. Numerous complaints by new market entrants demonstrate the necessity of initiatives by the regulatory authority to ensure fair competition and cost-based charges for monopoly services.

A clear schedule for the preparations of competition in the market for fixed voice telephony has not yet been established.

As far as the State-owned Cyprus Telecommunication Authority (CYTA) is concerned, the bill providing for its transformation into a joint stock company has not yet been adopted, pending consensus in Parliament.

The Cypriot postal services market is a *de facto* liberalized market.

Conclusion

In its 1998 Regular Report, the Commission concluded that significant measures towards approximation of legislation and market opening within the telecommunications and postal sectors were needed in order to bring them in line with the *acquis*.

Since the Regular Report of 1998, Cyprus has made progress, especially over the two last years, in preparing a general legal framework for harmonisation and has initiated the establishment of an independent regulatory authority. As for the liberalisation of the markets for electronic communications, only the provision of Internet services has been opened to competition. Implementation of the *acquis* and establishment of the regulator's office are progressing very slowly.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. Cyprus is generally meeting the commitments it has made in the accession negotiations.

In order to complete preparations for membership, Cyprus's efforts now need to focus on full liberalisation of the markets and the completion and implementation of the regulatory framework.

Chapter 20: Culture and audio-visual policy

Progress since the last Regular Report

There have been developments in Cyprus since the last Regular Report in the field of **audio-visual policy**, although there is no progress in legislative alignment to report. However, the Cyprus Radio Television Authority (CRTA), having established criteria to determine which events should be considered as of major importance for the public in Cyprus, drew up a list of such events.

Cyprus has continued to develop its administrative capacity to implement the Radio and Television Stations Law. The CRTA prepared a report on compliance by Cypriot broadcasters with the legal provisions concerning the broadcasting of a majority proportion of European audiovisual works, according to which all free-to-air national

stations comply with the relevant legislation. In addition, the CRTA has been particularly active on issues such as the protection of minors from potentially harmful content in broadcasts.

Cyprus has taken steps for the participation in the Media Plus and Media Training Community programmes as of 2003.

In the field of **culture**, no particular developments are to be reported. Negotiations are underway for the participation of Cyprus in the Culture 2000 Programme.

Overall assessment

Although further adjustments are still needed, Cyprus is largely in line with the *acquis* in this field. Administrative capacity has been enhanced by recruitment of staff and the allocation of additional resources such as new offices.

Cyprus is party to the Council of Europe Convention on Transfrontier Television and its amending Protocol.

Conclusion

In its 1998 Regular Report, the Commission concluded that Cyprus' audio-visual legislation was aligned with the 1989 audio-visual *acquis* following the entry into force of the audio-visual law in January 1998, but some discrepancies remained, however, with respect to the 1997 amendments to the *acquis*.

Since 1998, Cyprus has made significant progress. Cyprus is now well advanced regarding the implementation of European Audio-visual Policy and is largely in line with the *acquis*. The necessary administrative structures are in place.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this field. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts should now focus on adopting the necessary legislative amendments, especially concerning definitions, television advertising and teleshopping to finalise alignment with the *acquis*. It should continue its efforts to ensure the proper functioning of the relevant administrative bodies.

Chapter 21: Regional policy and co-ordination of structural instruments

Progress since the last Regular Report

Since the last Regular Report, significant progress has been made in preparing for the implementation of structural policies.

Concerning **territorial organisation**, a proposal by the Statistical Service of the Republic of Cyprus was accepted in February 2002 by Eurostat, regarding the provisional NUTS classification in Cyprus. The proposal provides that the Republic of Cyprus is designated as a provisional single unit at NUTS levels I, II and III. The administrative

districts are proposed to be provisionally classified at NUTS level IV and the local authorities, i.e. Municipalities and Community Councils, at NUTS level V.

The designation of the areas facing structural difficulties, eligible for Objective 2 status, is in process.

There have been no particular developments since the last Regular Report regarding the **legislative framework**.

Concerning **institutional structures**, and the management of structural actions, the overall division of competencies regarding the programming and implementation of Structural Funds and the Cohesion Fund was approved by the Council of Ministers, including the detailed definition of tasks of the Planning Bureau, which has been designated to be the Managing Authority for all Single Programming Documents and the Cohesion Fund and is in charge of the co-ordination of programming of Structural Funds assistance, the Paying Authority (Accounting and Financial Services Directorate of the Treasury), and the intermediate bodies. The Structural Funds Unit of the Planning Bureau is co-ordinating all remaining preparatory activities for designation and setting up the implementation system.

With regard to **programming**, in April 2002 the Council of Ministers has decided to prepare 3 Single Programming Documents for Objective 2, Objective 3 and Fisheries. A guidance note has been sent to all services concerned and tendering procedures launched for external experts to support ex-ante evaluation of all programming documents. Furthermore, an inter-ministerial committee for programming and the management of Structural Funds, a subcommittee for each programming document and a consultative programming committee have been set up in April 2002. As to the preparation of INTERREG, the first crossborder programme with Greece has been approved by the Commission in March 2002.

As regards the **partnership principle**, the Monitoring Committee was designated.

In the field of **monitoring and evaluation**, the implementation Plan for setting-up a system for the management of Structural Cohesion Funds was finalised and submitted to the Accession Conference in March 2002.

With regard to **financial management and control**, an Internal Audit Board was established by a Council of Minister's Decision in January 2002. The Internal Audit Board is chaired by the Minister of Finance with participation of the Minister of Health, the Minister of Communications and Works, the Accountant General and a qualified accountant from the private sector.

As regards **statistics**, compilation of regional data for analysis, evaluation and monitoring has continued.

Overall assessment

Cyprus has already organised its territory into units corresponding to the NUTS classification.

Cyprus is well advanced as regards the setting up of *institutional structures*. It has designated the bodies, which are to be responsible for the implementation of the

Structural and Cohesion Funds. However, the functions and responsibilities of different bodies of the main authorities, which will be responsible for ensuring compliance of operations financed by the Funds, still have to be detailed, taking into account the principle of separation of functions. Project selection and decision-making should be managed within a framework that ensures transparency, efficiency and reliability in the implementation of programmes. Cyprus should also continue to work towards developing the necessary structures and co-ordination mechanisms to manage financial assistance from the European Social Fund in the context of the European Employment Strategy and the inclusion process.

With regard to *programming* Cyprus's decision to opt for Single Programming Documents is an important step forward. However, efficient inter-ministerial co-operation and partnership will need to be ensured through the whole process of preparing the Single Programming Documents, which Cyprus envisages to submit to the Commission in March 2003.

In the field of *monitoring and evaluation* work on ensuring compliance with the *acquis* requirements for evaluation needs to continue, in particular as regards the ex-ante evaluation of the Single Programming Documents. The development of an appropriate information technology (IT) system has to be enhanced.

Cyprus has generally a good system in the field of *financial management and control*, but has to finalise the specific procedures for financial control, auditing, certification of expenses and correction of irregularities applicable to the Structural and Cohesion Funds. Multi-annual programming of budgetary expenditure is already being implemented in Cyprus. As far as the management information system is concerned, difficulties in the development of the new computerised financial information and management accounting system (FIMAS) have to be overcome. This system has to be fully operational by the time of accession.

As for *statistics*, the key indicators necessary for the management of the Structural Funds are available at national level. As regards regional statistics, efforts need to be pursued to bring them up to the level required for programming, in particular in the future Objective 2 areas.

Conclusion

In its 1998 Regular Report, the Commission concluded that the regional disparities between the northern and southern part of the island had further increased. The implementation of structural funds would have to address these disparities when a political solution was found.

Since the 1998 Regular Report, due to the economic crisis in the northern part since 2000, the income gap with the southern part of the island has been aggravated. A political settlement on the basis of which these disparities could have been addressed has not yet been found. Meanwhile, the southern part of Cyprus has continued to make important progress in aligning with the *acquis* and preparing for participation in structural instruments, and few problems have been encountered. Cyprus has reached a good level of alignment with the *acquis* and is well advanced with respect to administrative structures.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. It is generally meeting the commitments it has made in the accession negotiations in this chapter.

In order to complete preparations for membership, Cyprus's efforts should now focus on further preparing its Single Programming Documents. Therefore, it needs to seriously increase the resources devoted to this process. Furthermore, Cyprus needs to focus on improving the final implementation structures and reinforcing their administrative capacity, and reinforcing systems and procedures for effective monitoring, financial management and control to enable the management of the Cohesion and Structural Funds.

Chapter 22: Environment

Progress since the last Regular Report

Since the last Regular Report, Cyprus has made legislative progress through the adoption of important laws, and it has somewhat strengthened its administrative capacity to implement and enforce the environmental *acquis*.

Cyprus has continued the **integration of environment into other policies**. The enactment and implementation of the Environmental Impact Assessment Law has proved an effective means to integrate environmental concerns at the project level. In agriculture, measures have concentrated on the appropriate use of fertilisers and pesticides and the setting up of the legal framework for the promotion of organic cultivation. In energy, the main measures related to encouraging the development of renewable energy sources (primarily solar and wind), promoting energy efficiency measures in all sectors and the preparation of the strategy to address greenhouse gas emissions. The main activities for industry concentrated on assisting and encouraging small businesses and plants to adopt more environmentally friendly approaches, through a wide range of fiscal measures, and the promotion of the European Environmental Management and Audit Scheme (EMAS) and international environmental standards. In the transport sector, the new strategy on sustainable mobility is reflected in the new land use plans for urban areas.

Cyprus has completed transposition of **horizontal legislation**. It proceeded with the full implementation of the Law for the Environmental Impact Assessment (EIA) of certain projects in February 2002.

In the field of **air quality**, an amendment to the Type Approval of Motor Vehicles Law was made in March 2002, incorporating the necessary changes so that non-road mobile machinery is now covered. Also, the type approval of vehicles, their trailers and their separate technical units regulations were adopted under the above law in March 2002. Cyprus has proceeded with the programme for the full compliance of existing service stations by January 2003. At the moment 70 petrol stations (out of a total of 241) have installed the equipment required for vapour recovery under the Directive on volatile organic compound emissions. Regulations amending existing Regulations under the Petroleum Law have been approved in July 2002. As a party to the Kyoto Protocol to the UN Framework Convention on Climate Change since 1999, Cyprus proceeded in December 2001 to assess the ambient air quality and draw up zones of pollution in accordance with the EU Ozone and Air Framework Directives.

In the field of **waste management**, the Law on Packaging and Packaging Waste and its set of implementing Regulations were enacted in April 2002. In May 2002, regulations were adopted regarding PCBs/PCTs, waste oils, and batteries and accumulators. Also worth noting is the establishment of a waste oil regeneration plant that began operation recently.

As regards **water quality**, the Water Pollution Control Bill transposing a number of water quality directives was adopted in June 2002. Two sets of Regulations, on the limitation of water pollution from asbestos and the management of sewage sludge, were approved in May 2002. The areas which are used or intended to be used for drinking water abstraction have been identified and mapped. A monitoring programme has been put in operation, which is in line with the *acquis* requirements for the minimum necessary microbiological parameters, and with most of the chemical parameters, for drinking water. For bathing waters, 105 fixed coastal stations were monitored and quality analysis of the data has shown full compliance with the relevant Directive. Prosecution was initiated against 3 companies whose effluents do not comply with the terms and conditions set in the permits issued according to the Water Pollution Control Law.

In the field of **nature protection**, Cyprus has submitted the technical data sheets for the habitats and species proposed for technical adaptation of the Birds and Habitats Directives. In October 2001, Cyprus ratified the Barcelona Convention Protocol concerning Specially Protected Areas and Biological Diversity in the Mediterranean, and the Protocol for the Protection of the Mediterranean Sea against Pollution from Land-Based Sources. The *acquis* on wild animals in zoos was also adopted. Projects for the protection and conservation of the endangered bird of prey *Gyps fulvus*, and for the protection of the endemic water snake *Natrix natrix cypriaca* also started in the period covered by this report. Unfortunately, the development of the Larnaca airport by the BOT method (Build, Operate and Transfer) grants the investor the right to construct and operate an airport hotel in the Salt Lake area, which is listed as an environmental heritage area under the Ramsar Convention.

With regard to **industrial pollution control and risk management**, relevant regulations under the Health and Safety at Work Law were enacted in December 2001 on the control of major accidents and hazards. As regards the issuing of permits, Cyprus has opted for a system of several fully co-ordinated permits rather than one integrated permit. However, certain provisions of the Directive on Integrated Pollution Control (IPPC) were incorporated in the new Water Pollution Control Act of June 2002 and preparations for the transposition of the IPPC Directive have continued.

In the field of **chemicals and genetically modified organisms (GMOs)**, a law amending the Dangerous Substances Law together with implementing regulations were passed by the House of Representatives in May 2002. The bill transposing provisions of the Directive on deliberate release into the environment of Genetically Modified Organisms was submitted to the House of Representatives in November 2001 where it remains for the moment.

As regards **noise** from vehicles and machinery, the new framework law for all the New Approach Directives was enacted in April 2002. The bill on noise from household appliances was approved by the Council of Ministers in July 2002.

As regards **nuclear safety and radiation protection** (*see also chapter 14 – Energy*), a new ionising radiation law, the Radiation Protection Law, and a Regulation regarding the information to the public in case of radiological emergency were approved in June and July 2002 respectively.

Cyprus has further strengthened its **administrative capacity**. The Environment Service has been allocated 6 additional employees. The option of purchasing services from the private sector was made available to public agencies. Measures were taken for the testing and examination of vehicle exhaust emissions. The inspection of the majority of public vehicles has been completed. Seminars and other similar events with an informative and training character have been organised.

Cyprus's 16 implementation programmes on CO₂ strategy, ozone substances strategy, waste management strategy, environmental information, IPPC and chemical substances, habitats, EMAS, PCPs, nitrate pollution, design of the Paphos landfill, packaging, hazardous waste, landfills assessment, and waste water systems design are well under way.

Overall assessment

Cyprus has achieved considerable alignment with the EC environmental *acquis*. In order to complete alignment, measures need to be adopted in the fields of air quality (adoption of the Atmospheric Pollution Control Bill and the Air Quality Bill, a new law on fuel quality and one set of implementing regulations have to be urgently put into force), waste management (Bill on Hazardous Waste Management), water quality (Water Entity Bill and measures transposing the *acquis* on dangerous substances, on bathing water, shellfish waters, and on fresh waters supporting fish life), industrial pollution control and risk management (enactment of Bill on Integrated Pollution Prevention and Control, Seveso II), chemicals and genetically modified organisms (Bill on GMOs and Regulations), noise (equipment for use outdoors).

Cyprus has ratified the Kyoto Protocol in 1999.

The principle of integration requires continuous attention both at national and at Community level. Cyprus needs to continue integrating environmental protection requirements into the definition and implementation of all other sectoral policies so as to promote sustainable development.

The most worrying issue in Cyprus relates to waste management. In addition to completion of transposition, practical measures in order to secure full compliance with the *acquis* still have to be prepared on the basis of an assessment of current landfills, which has been initiated. All current landfill sites have been identified and a four-year programme regarding closure or upgrading has been prepared. Other issues which require attention relate to the strategy to reduce greenhouse gas emissions (still needs to be approved by the Council of Ministers), the implementation of the *acquis* relevant for the combustion plant at Vassilikos and Dhekelia and the finalisation of the inventory of all radiation sources.

Considerable investment needs to be secured in the medium term, to ensure implementation of the environmental *acquis*.

As regards *administrative capacity*, the fragmented structure of responsibilities means that the capacity to implement the EC environmental *acquis* still requires attention. A high level of co-operation between departments needs to be ensured. Over the pre-accession period efforts have been made to strengthen human resources with the recruitment of qualified staff. The use of non-permanent staff and the purchase of private sector services have overcome shortfalls in manpower. Staffing levels remain a problem in some sectors, in particular as regards air quality, waste management and IPPC, but in general personnel working in the field are well-qualified and demonstrate a high degree of motivation.

Cyprus has in general terms made the technical resources available to enable the administration to perform its duties, but it should pursue contacts with Member States so as to benefit from their experience. On strategic planning, the system established under the authority of the Planning Bureau appears to provide a sound basis for co-ordinating the harmonisation efforts.

Responsibilities for permitting, monitoring enforcement and inspection are relatively fragmented. The enforcement capacity remains under-resourced in a number of areas, such as IPPC, and needs to be strengthened. In nature protection, recent efforts have been made to strengthen enforcement of existing laws and an increased number of offenders are being prosecuted, a trend that needs to be continued.

Conclusion

In its 1998 Regular Report, the Commission concluded that Cyprus still needed to transpose most of the EC environmental legislation. The adoption of the environmental *acquis* could only be successful if the existing environmental management structures were substantially strengthened and if the levels of public and private investments were increased, especially in the air, waste and water sectors.

Since the 1998 Regular Report, Cyprus has made steady progress in aligning legislation as well as strengthening the administrative capacity, in particular in the past two years.

Negotiations on this chapter have been provisionally closed. Cyprus has been granted transitional arrangements with regard to packaging and packaging waste (until 31 December 2005), for urban waste water treatment (until 31 December 2012), for sulphur content of certain liquid fuels (31 December 2004), and for air pollution from large combustion plants (special provisions). Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on finalising transposition (air quality, waste management, water, industrial pollution, chemicals and genetically modified organisms) and on the landfill of wastes.

Chapter 23: Consumers and health protection

Progress since the last Regular Report

During the reference period Cyprus has made progress in the consumer protection area.

No particular developments can be reported with respect to **safety related measures**.

With regard to **non-safety related measures**, certain minor amendments of the Product Liability Law were made to further align with the *acquis*. The Consumer Credit Law, which was enacted already in March 2001, came into force in June 2002. An amending legislation to the Defective Product Law 1995-2000 was adopted in April 2002 and entered into force in May 2002.

Concerning the **functioning of the market surveillance mechanism**, the Competition and Consumer Protection Division of the Ministry of Commerce, Industry and Tourism is the competent national authority in the field of consumer protection, assuming responsibility for the effective protection of the health and safety and the economic interests of the consumer as well as consumer information.

The staff of the Competition and Consumer Protection Division has participated in various courses and workshops on general product safety, distance selling, advertising and package travel. Another series of seminars dealt with consumer credit.

The Cyprus Consumers Association remains dependent on a state grant, which for the year 2002 has been increased to CY£ 40 000 (€ 69 444).

A contribution to consumer education and information activities has been made through the publication and distribution of informative brochures.

Overall assessment

Transposing measures covering all areas of the consumer protection *acquis* have been adopted and legislative transposition is at an advanced stage. Activities concerning products covered by the General Product Service Directive are well established in Cyprus. In relation to the relatively small territory and the number of citizens, the present system is quite efficient and generally meets consumers' needs.

The funding of public testing laboratories should be subject to a thorough review. Their role should be reconsidered in order to allow more open access for the private sector and to give them the opportunity to have their products tested even before they are marketed.

The Cyprus Consumers' Association continued its educational campaigns but needs to intensify its activities in promoting consumer interest in public life.

In general, a stronger involvement of institutions other than the Ministry of Commerce, Industry and Tourism, the Competition and Consumer Protection Division and of associations and parties interested in consumer issues is needed, and responsibility for actions should be shared.

Conclusion

In its 1998 Regular Report, the Commission concluded that, despite good progress having been achieved, efforts were still needed in order to ensure full harmonisation of legislation and its enforcement.

Since the 1998 Regular Report, Cyprus has continued to make good progress, and few problems have been encountered. The *acquis* is being implemented rather satisfactorily by the Competition and Consumer Protection Division. However, it will be necessary to

strengthen the administrative capacity of this Division and in particular increase its staff. Overall, Cyprus is at an advanced stage in terms of legislative alignment and administrative capacity.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements. Cyprus is generally meeting the commitments it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus's efforts now need to focus on strengthening the administrative capacity of the main structures in charge of enforcing the *acquis*. All interested parties, such as consumer associations, must be involved in market surveillance activities. A new definition of the scope and work-plan of the Advisory Committee on consumer issues would be advisable.

Chapter 24: Co-operation in the field of justice and home affairs

Progress since the last Regular Report

During the period covered by this report Cyprus made further progress in this field.

In the field of **data protection**, Cyprus ratified the Council of Europe Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data, and the respective national legislation entered into force in November 2001. The Office of the Commissioner for Data Protection was established. It currently benefits from three highly qualified officers to assist the Commissioner and three support staff. These posts so far are temporary ones (*see chapter 3 - Free movement of services*).

As regards **visa policy**, further legislative alignment was achieved notably through introduction of the Airport Transit Visa, introduction of a visa obligation for nationals of seven countries (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates, and Zimbabwe) in alignment with the EU visa obligations, abolition of the visa obligation for nationals of Bulgaria and Israel, and revocation of bilateral agreements with Bulgaria, Israel and Lebanon for the issuing of visas at the borders. With Syria, agreement was reached on the effective date for the revocation of a similar agreement, i.e. on 15 October 2002.

Cyprus has started to upgrade a number of embassies and consulates in order to react effectively to the increased workload for the issuing of visas. By September, over 15 additional officers had been posted in Cyprus' embassies.

Concerning **external borders** and the **Schengen** *acquis*, a comprehensive study by an *ad hoc* Committee set up by the Cypriot authorities on the structure of the Police was concluded in January 2002. The study recommends bringing all the police units dealing with external border control under the same command and limiting the transferability of officials.

In the field of **migration**, there was alignment with the *acquis* in December 2001 as regards admission of third country nationals for study purposes and for self-employment and in June 2002 as regards the adoption of practices followed by Member States concerning expulsion through amendments to the Aliens and Immigration Regulation.

A readmission agreement was signed with Italy in June together with another agreement on co-operation in sea surveillance for combating illegal migration in the Eastern Mediterranean. In July, a readmission agreement was signed with Lebanon. Contacts have been established with Portugal, Romania, Egypt and Syria with a view to negotiating readmission agreements.

As regards **asylum**, further alignment has taken place. The Refugee Law amendment introducing the Independent Review Authority and the concept of countries where there is no risk of persecution and implementing regulations were enacted. The Refugee Authority took up its functions as of January 2002 and has started to take the first decisions. The Asylum Law of 2000 and the amendments adopted in 2002, and the Cyprus Constitution duly incorporate the *non-refoulement* principle.

In the field of **police co-operation and the fight against organised crime**, Cyprus aligned its domestic law with the Joint Action of 1998 making it a crime to participate in a criminal organisation through an amendment to the criminal code which entered into force in March 2002.

As regards the **fight against terrorism**, the International Convention for the Suppression of the Financing of Terrorism was ratified in November 2001. The Unit for Combating Money Laundering (MOKAS) has been assigned to the examination of measures against financing of terrorism.

As regards the **fight against fraud and corruption**, the Council of Europe Criminal Law Convention on Corruption entered into force in Cyprus in July 2002 (*see also section B.1.1. - Democracy and the rule of law*).

Concerning **drugs**, Cyprus has submitted its application for participation in the European Monitoring Centre for Drugs and Drug Addiction (EMCDDA). The draft agreement has been accepted by the Cypriot authorities. The bill for the establishment of the National Focal Point for the participation in the EMCDDA was enacted in July 2002.

As regards **money laundering**, 11 posts were created for the Unit for Combating Money Laundering (MOKAS) of which 2 were for lawyers, 8 for investigators (accountants and financial analysts) and one for supporting/administrative staff. Recruitment started in July (*see also Chapter 4 - Free movement of capital*).

In the field of **customs co-operation**, Cyprus ratified the Protocol on Mutual Administrative Assistance on Customs Matters between Cyprus and the EC in December 2001.

Concerning **judicial co-operation in criminal and civil matters**, the European Convention on the Transfer of Proceedings in Criminal Matters entered into force in March 2002. The law for the statutory introduction of legal aid, which includes family law cases was approved in July 2002.

Overall assessment

Cyprus is at the initial stage of setting up the office of the Commission for the Protection of **Personal Data**. It should ensure that it has the necessary technical equipment and staff to be operational in full independence and without external political interference. The

Independent Supervisory Authority should also be rendered fully operational and able to fully exercise its duties.

As regards **visa policy**, Cyprus should continue the alignment of its legislation with the Common Consular Instructions. To complete the alignment with the EU visa obligations list, nationals of the Russian Federation and the Federal Republic of Yugoslavia must be removed from Cyprus's visa-free travel list. A diplomatic mission should be established in Qatar or a temporary alternative solution should be found to facilitate the issuing of visas for nationals of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

Cyprus has to terminate the practice of issuing visas at the borders for members of tourist groups.

Cyprus must terminate, by accession at the latest, the practice of granting visas onboard the ships.

Concerning **external borders** and the **Schengen *acquis*** two of the existing bilateral Merchant Shipping agreements (China and the Philippines) should be renegotiated with a view to alignment with the *acquis*.

Concerning the Schengen *acquis*, Cyprus is continuing its preparations by fully implementing the existing Schengen Action Plan and by developing the National information system. However, efforts for the preparation towards SIS II will have to be made in order to avoid technical problems and delays.

At airports, plans for Schengen separation are ready. New terminals are to be in place by the year 2005 (at Pafos) and 2006 (at Larnaca). Training is provided to all passport controllers. The equipment for document checking meet the standards. The Cypriot Immigration Police is familiar with the Schengen Catalogue, which has been introduced in different seminars and distributed to border crossing points.

At the ports, a high level of border controls should be ensured by accession, particularly in relation to the obligation of checking every person face to face when crossing the external border. The embarking and disembarking procedures are not fully in alignment with the *acquis*. The Cypriot authorities must decide how to ensure a fully compatible Schengen checking system. The reconstruction of the terminal, which is planned for 2005, would seem the simplest and most economical solution to meet the Schengen standards. Also, the route between the terminal and the ships should be made hermetic, preferably by physical isolation.

The enhancement of equipment for border surveillance (radar network, helicopters, patrol boats) must continue without further delays. Given Cyprus's geographical situation and the methods used for illegal immigration and human smuggling, the radar network, supported by information provided by mobile units such as helicopters and patrol boats, is a necessary device for proper blue border surveillance. The lack of these instruments could also hamper the lifting of internal border controls after accession to the EU. So far, Cyprus has purchased thermal night vision equipment for two Marine Police vessels and for two helicopters of the Police Airwing but the acquisition of other equipment, i.e. 3 new helicopters and coastal radar surveillance, is still under discussion. As regards the purchase of equipment for customs controls, the relevant Department has acquired 3 gamma radiation detectors and a digital camera.

As regards **migration**, Cyprus should devote close attention to the conclusion of the negotiation of readmission agreements with Member States and also with the countries of origin of illegal immigrants. It should strengthen and implement measures to combat illegal employment and implement relevant sanctions against employers who employ third country nationals without a work permit. Concerning the adoption of uniform residence permits and standard expulsion documents, it is noted that amendments to the Aliens and Migration Regulations are required to this effect.

As regards **asylum**, an amending law which aims to introduce the harmonised concept of manifestly unfounded claims and the rights of recognised refugees, in line with the London resolution and the Geneva Convention, is pending. The Refugee Authority has hitherto dealt with 26 cases, almost all considered as manifestly unfounded. Due to the limited number of case-workers employed at the Asylum Unit (four) and the expected pace of work, the present production predictions could result in a backlog by the end of the year. Cyprus must ensure that the principle of *non-refoulement* is respected and that asylum claims are properly processed, facilitate the local integration of refugees and complete the building of a reception centre in order to increase reception capacity for asylum-seekers. Due attention will need to be paid to actual living conditions including health, education and occupational activities in this reception centre.

In the field of **police co-operation and the fight against organised crime**, Cyprus needs to establish a comprehensive strategy for fighting against new types of organised crimes and offences, and establish a special complaint unit inside the police for the fight against corruption. It needs to implement the conclusions of the study on the structure of the police.

In 2001, the Department of Customs and Excise and the Police signed a Memorandum of Understanding concerning co-operation in the fight against drugs. Co-operation between police, customs and maritime authorities, based on Memoranda of understanding, is good.

Negotiations with Europol for the conclusion of a bilateral co-operation agreement are underway.

Cyprus must ratify the Convention on Mutual Assistance in Criminal Matters and amend the Law on Acquisition and Possession of Weapons.

Statistical instruments for measuring crime rate should be improved, while new methods of technical crime investigation, including development of forensic investigation should be further developed.

Cyprus has signed but not ratified the 2000 UN Convention against transnational organised crime (Palermo Convention) and its three protocols.

As regards the **fight against fraud and corruption**, Cyprus put in place the necessary legislation with regard to the protection of EC financial interests already in 1998. Ratification of the Civil Law Convention on Corruption that was signed in November 1999 is still outstanding. Cyprus's application to join the OECD Convention on Combating Bribery of Foreign Officials in International Business Transactions is pending.

Cyprus should pay more attention to the fact that prevention through transparency and accountability standards is as important as repressive tools.

Preparation for the participation of Cyprus in the European Information Network on **Drugs** and Drug Addiction (Reitox) and EMCDDA needs to be reinforced through the setting up of a National Focal Point and the development of a national drugs strategy.

The 1996 Act provides an efficient basis for dealing with **money laundering**. The Unit for combating Money Laundering (MOKAS) has been operational since 1997. MOKAS currently has 8 staff members with investigative powers (3 prosecutors, 4 police investigators and one customs officer) and the Head of the Unit. The Unit co-operates with the Police and Customs and Excise. 3 customs officers who are part-time employees assist the Customs Officer of MOKAS. The ongoing recruitment of the approved additional staff should be completed without delays.

Cyprus maintains close international co-operation in this area. MOKAS strongly supports international co-operation and to this end gives priority to requests for legal assistance submitted by foreign authorities.

It is clear from the statistics that there has been a significant increase in the rate of reporting of suspicious transactions by financial institutions, which demonstrates that there is a growing awareness of money-laundering issues. Although the statistics in relation to confiscation orders are modest, it is hoped that with the progress of cases in Court, the numbers of such orders will increase.

Cyprus must bring its law into alignment with the *acquis* as regards existing accounts when the beneficiary has not been identified.

The implementation of the **co-operation between customs authorities** and business organisations should now be ensured by concluding Memoranda of Understanding with business organisations. Cyprus should also start preparations for accession to and implementation of the Convention on Mutual Assistance and Co-operation between Customs Administrations and improve the effectiveness of customs controls in harbours and customs warehouses as well as in the tax-free zones.

As regards **judicial co-operation**, Cyprus should take further measures to ensure implementation of the Community instruments in the area of judicial co-operation in civil matters, notably as regards mutual recognition and enforcement of judicial decisions. Direct contacts between competent judicial authorities should be made possible.

With the ratification of the European Convention for the Protection of Individuals with regard to Automatic Processing of Data, Cyprus is a party to all **human rights** instruments under the justice and home affairs *acquis*.

Conclusion

In its 1998 Regular Report, the Commission concluded that Cyprus had made progress, especially in combating money laundering, drugs trafficking and illegal immigration and added that it should press ahead with its efforts. Cyprus would have to adopt the international laws relating to civil and criminal procedures without delay and ensure that rules on asylum and immigration were applied to EU standards.

Since 1998, Cyprus has made steady progress in many areas to ensure legal harmonisation and create the necessary structures and procedures. It has first made progress in the field of immigration, and subsequently on asylum and the fight against fraud and corruption through the setting up of an institutional framework. The legal framework and required administrative structures are now largely in place.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this field. Cyprus is generally meeting the commitments it made in the accession negotiations.

In order to complete preparations for membership, Cyprus's efforts should now focus on completing legislative alignment (visas, asylum), and on improving the administrative capacity in general. More specifically, the recruitment of the staff for MOKAS should be completed. It must ensure proper implementation of the *acquis*, especially in the asylum and migration field and in the fight against money laundering, fraud and organised crime, as well as control of external borders.

Chapter 25: Customs union

Progress since the last Regular Report

Since the last Regular Report, Cyprus has achieved further progress.

Concerning **alignment with the customs *acquis***, in May 2002 the House of Representatives enacted the amendment of the Customs and Excise Law with regard to customs warehouses, inward processing and temporary importation. Implementing legislation aligned with the Community Customs Code was enacted in July 2002.

Since the beginning of 2002, Cyprus has adopted and implemented the provisions regulating duty reliefs on pharmaceutical products.

The law on intellectual property rights (counterfeit and pirated goods) was enacted in March 2002 and came into force the following month.

As regards **administrative and operational capacity**, the Department's Business Strategy for Customs 2001-2003 and the Departmental Management Plan (DMP) for 2002 are being carried out. The DMP sets out, for each unit in the Customs department, detailed actions to be undertaken, including the time schedule and the foreseen targets. Concerning computerisation, the Cypriot Customs Department has developed detailed plans in order to achieve a satisfactory level of IT operational capacity by the accession. The first phase of the computerisation of the Department of Customs and Excise started in September 2001 on the basis of the adaptation to Cyprus of the Danish Customs Administration IT system. In the reporting period, Cyprus has implemented the integrated tariff and quota management modules of its information technology system.

Concerning training, the Training and Developing Strategy for 2001-2003 is being implemented. Two training rooms have been constructed at Nicosia and Limassol customs stations and two more are currently being prepared for Larnaca port and Larnaca airport stations.

Regarding the recruitment of new staff, 25 new posts for customs inspectors have been created over the reporting period. A Customs Co-operation Committee has been set up to facilitate the provision of information about legislative, policy and procedural changes to economic operators and members of the public.

Overall assessment

Cyprus customs will have to adapt its implementing rules and systems management, which are different in detail from those of the Community. Further legislative alignment is needed in particular concerning inward processing, temporary importation, outward processing, origin and binding origin information, customs clearance, re-importation, national transit, simplified procedures, export, cultural goods, duty reliefs, entry procedures, customs debt, free circulation, customs warehousing, binding tariff information, free zones and free warehouses. Moreover, the full range of Community commercial policy measures and export refunds will not apply until accession, and these affect the context in which the provisions in areas such as non-preferential origin, inward and outward processing are applied.

In the area of Risk Analysis, the Department has developed and introduced since 2000 a National Risk Assessment Document in order to provide risk analysis guidelines on all aspects of custom control. This document has been regularly reviewed and updated. The Cypriot customs administration should further strengthen the application of post-clearance controls and the system of risk analysis.

As regards computerisation, Cyprus is applying an integrated tariff module and should be able to meet the interconnectivity requirements on time for EU accession through the implementation of the forthcoming phases of its computerisation project.

Conclusion

In its 1998 Regular Report, the Commission concluded that although Cyprus could count on a modern customs administration, it should reinforce its effort to align its customs legislation fully and prepare its customs services for the operation of all the customs procedures with economic impact, the system of tariff suspensions, the administration of tariff quotas and ceilings and the use of modern computerised systems.

Since 1998, although slowly in the first two years, Cyprus has progressed, especially in aligning its legislation on the *acquis* in this field although not to the extent considered necessary at this stage and has continued to enhance its administrative and operational capacity. Overall, Cyprus has a well-organised and well-functioning customs administration.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements. Cyprus is generally meeting the commitments it has made in the accession negotiations.

In order to be ready for membership, Cyprus now needs to focus its efforts on achieving full alignment with the *acquis* and proceed as planned with the information technology strategy in order to achieve interoperability. The adoption of the pending legislation in this area would see a significant advance in the level of alignment. Moreover, Cyprus should take the necessary steps to further enhance its administrative capacity to prepare

for the application of measures and provisions that are in the legislative process as well as those which will be introduced only at the time of accession.

Chapter 26: External relations

Progress since the last Regular Report

Since the last Regular Report, Cyprus has continued to align with the *acquis* on common commercial policy and to co-ordinate positions and policies within the World Trade Organisation (WTO) with the EU, in particular with regard to the Doha Development Agenda negotiations.

As regards the **common commercial policy**, upon accession Cyprus will be required to align its tariffs with those of the EC. Cyprus's applied tariffs currently average 9.6% (MFN) on all products, 32% on agricultural products, 10.2% on fishery products and 4% on industrial products. By comparison, EC tariffs currently stand at 6.3% on all products, 16.2% on agricultural products, 12.4% on fishery products and 3.6% on industrial products.

As regards export credits, the Cypriot system is in line with the OECD consensus and has achieved harmonization with the *acquis*.

In an effort to strengthen export controls concerning **dual use goods**, Cyprus has upgraded checks at all its ports during the previous year. Whatever the declared contents, each container leaving the country has now to pass a detecting pillar. Cyprus has signed a memorandum of understanding with the UK Customs and a number of other bilateral agreements of co-operation. Furthermore, officials of the Ministry of Commerce have participated in seminars, e.g. in the United Kingdom in November 2001, to improve their knowledge of export control standards.

As regards **bilateral agreements with third countries**, in April 2002 Cyprus signed an agreement with India to promote and protect investment and a new co-operation agreement with Malta.

Concerning **development and humanitarian aid**, the co-operation with international non-governmental organisations has continued. Humanitarian assistance from the three main sources for assistance i.e. the MFA, the Ministry of Finance and the Planning Bureau, will reach approximately € 26 m (CYP 1.5 million) for the year 2002 comprising multilateral assistance, UN Regular budget and voluntary contributions and humanitarian emergency assistance.

Overall assessment

The EU and Cyprus have established a framework for co-operation regarding the WTO issues both at ministerial and at departmental level. Cyprus has been supportive of EU policies and positions within the WTO framework in particular also during the preparation for and the launching of the Doha Development Agenda. This close co-operation should continue. Close co-ordination is needed and should continue to ensure the smooth alignment of Cyprus's GATS commitments with the EC's commitments and MFN exemptions and steps have been defined to this extent.

Cyprus is a signatory to the WTO agreement on information technology. Concerning the WTO Agreement on Trade in Textiles and Clothing (ATC), coordination has taken place within the third stage of integration under the ATC to align Cyprus' integration programmes with those of the EC.

Cyprus has not concluded any free trade agreements with third countries.

Some progress has been achieved in the field of dual use goods, although further alignment to the *acquis* remains necessary. Cyprus is requested to keep the EC informed of its progress in this area, including in terms of goods under control although full alignment to the *acquis*, in particular the general export authorisations, can only take place upon accession. If medium and long term export credits are provided, Cyprus has to undertake further efforts to align with the *acquis*.

The Trade Service of the Ministry of Commerce, Industry and Tourism bears the responsibility for the import/export licensing, the allocation of tariff quotas and ceilings and surveillance procedures. Additional personnel have been seconded to the existing Unit dealing with import licensing to cope with the anticipated increased requirements.

The administrative infrastructure which needs to be in place with respect to customs services is discussed in the chapter on customs union (*Chapter 25 - Customs union*).

Conclusion

In its 1999 Regular Report, the Commission stated that Cyprus's external trade regime was already substantially aligned with that of the EC. Cyprus accepted the Community *acquis* in respect of external relations and had expressed its willingness to work closely with the EC in the preparation of, and during the WTO Round with a view to aligning positions and policies as closely as possible.

Since 1999, Cyprus has continued harmonizing with the *acquis*, and has reached a good level of alignment.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. Cyprus is generally meeting the commitment it has made in the accession negotiations in this field.

In order to complete preparations for membership, Cyprus efforts now need to focus on finishing the process of legislative alignment, as well as on ensuring that the capacity exists to fully implement and enforce the *acquis* in this field upon accession.

Chapter 27: Common foreign and security policy

Progress since the last Regular Report

Since the previous Regular Report, Cyprus has continued to align its foreign policy with that of the EU.

Cyprus participates in the multilateral **political dialogue** and continues to participate actively in the Common Foreign and Security Policy (CFSP), including meetings at the level of Political Directors, European Correspondents and Working Groups.

Cyprus has shown a keen interest in the development of the European Security and Defence Policy (ESDP) as part of the CFSP, and has actively participated in all the meetings in EU + 15 format (i.e. with non-EU European NATO members and candidates for accession to the EU), at both ministerial and expert level.

Cyprus participated in the Capabilities Improvement Conference which was held in Brussels in November 2001 and announced the Republic of Cyprus's contribution of 30 policemen to the European Union Police force, 10 of which will be available for the Rapid Reaction Force. At the EU + 15 Defence Ministers meeting in May 2002, the Republic of Cyprus declared its commitment to contribute to the European Union Police Mission in Bosnia-Herzegovina.

Cyprus hosted the UN Committee for the Exercise of the Inalienable Rights of the Palestinian People, which was held in Nicosia in April 2002.

As regards **alignment with EU statements and declarations**, Cyprus has regularly aligned its positions with those of the Union and, when invited to do so, has associated itself with the Union's **common positions and joint actions**. Cyprus has continued its cooperation with the EU in international fora, such as the United Nations and the OSCE. During the last UN General Assembly meeting, Cyprus shared common positions with the European Union at a rate of 98 %.

Cyprus has also aligned itself with all the Common Positions of the European Union relating to the fight against international terrorism and had ratified or acceded to most of the international conventions on international terrorism. Following the terrorists attacks of 11 September 2001, Cyprus aligned itself with the Conclusions and Plan of Action of the extraordinary European Council in Brussels. It also ratified in October 2001 the International Convention for the Suppression of the Financing of Terrorism. Cyprus has ratified the Rome Statute establishing the International Criminal Code

Cyprus's legislative framework allows for its effective participation in the CFSP, especially regarding the implementation of negative measures/sanctions. Cyprus has continued to comply with **international sanctions and restrictive measures** imposed by the UN and the EU. In both cases, a Decision of the Council of Ministers on the basis of existing legislation such as the Law on Transportation, the Customs and Excise Law and the Law on Defence has been issued.

Overall assessment

Cyprus maintains good and constructive relations with all neighbouring countries in the Middle East. These relationships have allowed Cyprus to contribute to the effort to find lasting peace in the area, by facilitating meetings in Cyprus between Israelis and Palestinians and other parties and maintaining avenues of communication. Cyprus is an active proponent of regional co-operation in the Mediterranean basin and strives to contribute to regional stability in the framework of the Euro-Mediterranean Partnership. In addition, in May 2002, Cyprus accepted to accommodate for a week the 13 Palestinians who had been expelled from Bethlehem, thus allowing the Member States to find ways of admitting them into the EU. Bilateral relations with Russia have developed satisfactorily and remain stable. Due to the Cyprus problem the relations with Turkey remain sensitive.

Concerning administrative capacity to implement the provisions relating to the CFSP, Cyprus has a well-functioning Ministry of Foreign Affairs. It has the capacity to effectively participate in the Associated Correspondent's Network, both in terms of staffing allocations, and in terms of the appropriate information systems. The posts of Political Director and European Correspondent are well established.

Conclusion

In its 1999 Regular Report, the Commission stated that Cyprus had continued to orient its foreign and security policy towards the EU, was striving to contribute to regional stability in the framework of the Euro-Mediterranean Dialogue and had established strong co-operation with its Mediterranean neighbours.

Since 1999, Cyprus has made steady progress in aligning with the CFSP *acquis*; its legislative alignment is in general satisfactory at this stage and the administrative structures are in place.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements in this area. Cyprus is generally meeting the commitments it has made in the accession negotiations in this domain.

In order to complete preparations for membership, Cyprus's efforts now need to focus on ensuring that its foreign policy remains in line with the Union's developing foreign and security policy, adopting the legislation on economic sanctions and finalising the development of the necessary administrative structure.

Chapter 28: Financial control

Progress since the last Regular Report

Since the last Regular Report, Cyprus has made further progress in this field.

The **Public Internal Financial Control (PIFC)** system of Cyprus is under continuous revision. In terms of institution building, Cyprus has established centralised internal control and audit facilities within the Treasury/Office of the Accountant-General. During the past year special emphasis has been given to enhancement of the administrative capacity for the financial management of pre-accession aid and the enhancement of the functional independence of the Internal Audit Directorate (IAD), through the establishment of the Internal Audit Board (IAB) in January 2002. The functional independence of IAD is however not yet fully satisfactory and needs to be further strengthened, by reinforcing the responsibilities and authority of the Internal Audit Board (IAB).

During the period under review, the IAD completed the development of an Internal Audit Manual, an Internal Audit Charter, and the Strategic Plan (2002-2007). All are part of the set of documents that were sent to the Commission together with Cyprus's application for EDIS (Extended Decentralisation Implementation System for the management of pre-accession funds)

Furthermore, the IAD has prepared its first Annual Audit Plan (2002) which, together with the Strategic Plan, Manual and Charter, have been submitted to the IAB for endorsement.

Concerning **external audit**, a new legislation has been enacted which gives the right to the Auditor General to require any natural or legal persons receiving grants, guarantees or loans (the end-user of public funds) to provide proof of how the funds have been used.

As regards **control of structural action expenditure**, following the Government's decision of 2001 to designate the Accountant-General of the Republic and the Permanent Secretary of the Planning Bureau as National Authorising Officer (NAO) and National Aid Coordinator (NAC) respectively for the purpose of receiving EC funds, the National Fund (NF) has been set up within the Accounting and Financial Services Directorate of the Treasury. The NF Operational Manual and Audit Trail were completed and submitted to the Commission as part of Cyprus's application for EDIS (extended decentralised implementation). The gap assessment exercise which is the first step leading to EDIS has taken place in September 2002.

Meanwhile, the training of IAD personnel has continued in 2002 with participation by them in various seminars/courses. During the period under review, five qualified accountants were recruited for the IAD. 10 additional posts for qualified accountants have been approved in July 2002.

With regard to the **protection of EC financial interests**, an anti-fraud co-ordinating service has not yet been designated.

Overall assessment

Cyprus has a well-defined Public Internal Financial Control (PIFC) system to ensure that the financial management and control as well as the internal audit at its national budget spending centres (including foreign funds) is fully compatible with the relevant legislation, the budget description the principles of sound financial management and transparency in the use of the EC funds, and the protection of the financial interests of the EC. The establishment of permanent and sustainable training facilities for PIFC needs to be further monitored.

Furthermore, the administrative capacity of the Treasury will be further enhanced through continuous training and recruitment of new qualified staff and implementation of the new computerised Financial Information and Management Accounting System (FIMAS), which is currently being developed. The first phase is expected to be implemented by mid-2003, and the second phase by the end of 2003.

The criteria for compliance with international audit standards at the level of the Supreme Audit Institutions (SAI) are met to a large extent by the Auditor-General (AG) in Cyprus. The issues of functional, organisational and operational independence of the AG have been sufficiently covered. Its financial independence needs to be further enhanced since currently the relevant budget forms part of the overall government budget. However, the limited scope of public auditing still raises concern. The AG has no power to audit state-controlled companies. So far no formal "discharge" mechanisms have been introduced to discuss the AG's audit reports in Parliament. However, the reports are made public and discussed by the Public Accounts Committee, the Government being

required to follow up the recommendations and report on a regular basis. Auditing procedures are governed by internal "Audit Guidelines" issued by the Auditor-General. These are based on the INTOSAI standards and guidelines. Particular importance is to be given to efforts concerning the management of pre-accession funds (in particular in the framework of EDIS) and future structural funds.

As regards the protection of the Communities' financial interests, Cyprus needs to clarify which steps it intends to take in order to establish or designate an operationally independent anti-fraud unit, responsible for the co-ordination of all legislative, administrative and operational aspects of the protection of the Communities' financial interests. Once it has been designated, this anti-fraud co-ordinating structure or service should establish effective co-operation with OLAF as well as with all other Cypriot institutions and bodies involved in the protection of the Communities' financial interests.

Conclusion

In its 1998 Regular Report, the Commission concluded that proper public internal financial control seemed to have been established and that legislation provided for an adequate level of protection for Government public funds and the financial interests of the Community. Although the structures of financial control seemed to correspond to EC structures, the accounting internal control and auditing procedures needed to be strengthened.

Since 1998, Cyprus has made substantial progress in this field. It has developed management and control systems for receiving EC funds and has made progress in the structural modernisation of its financial control system. Overall, Cyprus has reached a satisfactory level of harmonisation in this field. However, further efforts are required to ensure functional independence of the Internal Audit Directorate.

Negotiations on this chapter have been provisionally closed. Cyprus has not requested any transitional arrangements. Cyprus is generally meeting the commitments it has made in the accession negotiations in the field of financial control.

In order to complete preparations for membership, Cyprus's efforts now need to focus on enhancing administrative capacity, in particular of the Treasury and of its anti-fraud structures, and actually starting the implementation of the Extended Decentralisation Implementation System (EDIS), once approved by the Commission.

Chapter 29: Financial and budgetary provisions

Progress since the last regular Report

Cyprus has made further progress in this area since the last Regular Report.

As regards the **national budget and EC co-financed measures** (basic budgetary legislation, medium-term budget expenditure, budget management of projects and programmes), no further developments can be reported for the period covered by this report.

In the sectors of the *acquis* having an effect on the EC's **own resources system**, Cyprus has further progressed.

In the field of GNP resources, progress can be recorded in the provision of GNP data in accordance with ESA-95. The European set of accounts, as well as the concept and definitions of the main aggregates, are being analysed and the relevant changes introduced, both in terms of methodology for estimates and scope of the survey data

Concerning the VAT resource, progress towards full alignment was made with the entry into force in February 2002 of the latest amendments to the VAT code (regulating the imposition, administration, collection and enforcement of VAT). As to the estimate of the weighted average rate for the VAT resource, efforts are being made by the VAT Service with support of the statistical service to improve the estimate of private consumption by drawing on alternative data sources such as the household budget survey to a greater extent.

As regards the Quarterly National Accounts, the necessary framework is being established. A provisional first set of data for the production side at constant prices was prepared for the period 1995-2001 and work is now progressing on preparing the expenditure side quarterly estimates.

As far as co-ordination of the own resources system is concerned, the Budget and Fiscal Control Directorate of the Ministry of Finance has been nominated as the co-ordination unit, and staff has been recruited.

With regards to institution building, the VAT service and the Department of Customs and Excise are further implementing their Business Strategy Plans 2001-2003, while the statistical service has been strengthened with 7 new posts in 2002. As regards control measures, the Department of Customs and Excise is enhancing its administrative capacity with Commission support with a special focus on the fight against fraud, customs debt and a database system on tariffs.

Overall assessment

Further efforts should be made with regard to each of the types of own resources. As regards the VAT resource, the Weighted Average Rate should be calculated in accordance with ESA95. More effective implementation of the customs legislation is needed to strengthen the traditional own resources. On the GNP resource, the quality of National Accounts and GNP calculations needs to be improved.

As regards administrative capacity in these fields, the Ministry of Finance's directorate on budget and fiscal control, is the co-ordinator of the proper collection, monitoring and payment of funds to and from the EC budget. It will have to recruit new officers when becoming a permanent structure. Training and upgrading of their information technology infrastructure (equipment and software) should continue. The customs and excise department is proceeding with its computerisation programme. The VAT Service aims to introduce computer systems to enable the electronic submission of VAT returns and the direct payment of tax, and facilitate risk-based selection, execution of audit (including computer audit), the monitoring of audit effectiveness and compliance management.

The Internal Audit Department is responsible for conducting all checks and enquiries concerning the establishment and provision of traditional own resources. No major problems are expected in Cyprus fulfilling the conditions related to the establishment, the

correct flow of data in the accounts, and making available of traditional own resources by the date of accession.

In addition to the need for central coordination for the proper collection, monitoring, payment and control of funds to and from the EC budget, administrative capacity should be strengthened in the relevant policy areas which are discussed elsewhere in this Report, including agriculture, customs, and regional policy.

Conclusion

In its 2000 Regular Report, the Commission concluded that overall Cyprus had established the necessary rules and procedures concerning its budget for medium term programming of expenditure as well as for evaluation and follow-up. However, these procedures needed to be strengthened.

Since then, Cyprus has proceeded with preparatory work. The budgetary system enabling it to meet Community requirements with regard to co-financing and multi-annual programming has been put in place. The administrative capacity of the services involved has been increased substantially, including the co-ordination aspects. Overall preparations for implementation of the *acquis* in the field of the national budget and EC co-financed measures are progressing well after the establishment of a single budget in 2000, but the effort needs to be sustained.

Negotiations on this chapter continue. Cyprus has not requested any transitional arrangements. Cyprus is generally meeting the commitments it has made in the accession negotiations.

In order to complete preparations for membership Cyprus's efforts need to focus on setting up effective instruments to combat VAT and customs duty fraud, and improving the management of the GNP resource and the traditional own resources. It should also transform the current temporary co-ordinating unit in the Ministry of Finance, into a permanent resources unit for the co-ordination of calculation, control, payment of own resources, and reporting to the EU.

4.2. General evaluation²⁸

Since the 1998 Regular Report, Cyprus has made substantial progress in the different areas of the *acquis*. The legislative alignment process has accelerated in recent years. Cyprus has continued to pay attention to implementation and enforcement structures.

Over the past year, Cyprus has further advanced with legislative alignment and has improved its position in relation to administrative capacity, in particular in the fields of social insurance, veterinary and phytosanitary inspections, pharmaceutical services, combating money laundering, ship inspection, inland revenue, planning, environmental services, consumer and health protection, and customs.

Overall, Cyprus has achieved a good degree of alignment with the *acquis* in most areas and is advanced towards reaching adequate administrative capacity to implement the

²⁸ See "Towards the Enlarged Union: Strategy Paper and Report of the European Commission on the progress towards accession by each of the candidate countries", COM (2002) 700.

acquis in a considerable number of fields, although further efforts remain to be made. Detailed plans have been agreed, in particular in the negotiations and in the Action Plan, to cover the remaining gaps.

There has been significant progress in the different areas of the internal market. As regards *free movement of goods* approximation has been completed in a number of sector-specific areas. The adoption of the framework legislation on the New and Global Approach principle, following an initial delay, has allowed substantial legislative progress and constituted an important step towards further alignment with the *acquis*. In the field of public procurement full alignment has not yet been achieved. Furthermore, efforts are still required for transposition of the *acquis* relating to the notification procedure, market surveillance and product safety. The newly established Company for Certification has reinforced the infrastructure for standardisation and certification, whereas Cyprus has to continue efforts to enhance its market surveillance systems. In the field of *free movement of persons* Cyprus has taken a major step by adopting the framework legislation on the recognition of professional qualifications. It has abolished inconsistencies as regards the co-ordination of social security systems and has reached a good level of administrative capacity. On *freedom to provide services* good progress can be reported in terms of harmonisation, in particular with legislation on insurance companies and banks, including offshore banks. Enhancement of administrative capacity should particularly continue as regards supervisory authorities in the field of financial services. The liberalisation of *capital movement* is on course to achieve full alignment by accession. Although the administrative capacity for combating money laundering has been further enhanced through the recruitment of additional personnel, Cyprus must continue sustained efforts in this domain.

As regards *company law*, Cyprus's legislative alignment with the *acquis* is at an advanced stage. With respect to intellectual and industrial property rights, further efforts are required to strengthen enforcement capacity in relation to border controls, combating piracy and counterfeiting. In the field of *competition* steady progress has been made in adopting anti-trust and state aid legislation. A substantial improvement in state-aid and in anti-trust enforcement is evident after years of standstill. The State aid monitoring authority and the fully independent authority for the protection of competition function well, but should be developed further.

Cyprus has reached a good level of legislative alignment in the field of *agriculture* and has taken significant steps as regards the establishment of the Common Market Organisations. However, the administrative capacity to implement and enforce the *acquis* needs to be further strengthened in this field. Due priority should be given to the preparation of the Integrated Administration and Control System. In the area of *fisheries*, legislation has been aligned to a reasonable extent. Administrative capacity is in place but needs to be further reinforced. Cyprus has continued its efforts to further reduce the number of fishing vessels under its flag, but its Fishing Vessel Register has not yet become fully operational. However, the relevant infrastructure for the establishment of the register has been introduced and the implementation mechanisms are under way.

The comprehensive tax reform, concerning both indirect and direct taxation, has moved Cyprus significantly forward in the field of *taxation*. Cyprus has also made important progress with developing the necessary administrative capacity and has reached an adequate level in this respect. Cyprus can also rely on a well-organised and well functioning *customs* administration. Further legislative alignment is needed concerning

inward and outward processing, temporary importation, cultural goods, and procedural aspects. The adoption of the pending and outstanding legislation in this area is urgently required in order to achieve this alignment.

Cyprus needs to focus on full liberalisation of the telecommunications markets, speeding up the implementation of the *acquis*, and the establishment of the regulator's office

As regards *Economic and Monetary Union* good progress can be reported, as the Central Bank has now become independent.

Legislation in the *transport* sector is largely in line with the *acquis*, but some legislation, in particular regarding aviation, remains to be transposed. Safety matters have been particularly improved by legislative alignment and strengthened administrative capacities. Efforts in the area of maritime transport need to be continued.

As regards *social policy and employment*, Cyprus has achieved substantial progress. Alignment with the legislative *acquis* needs to be completed in a few areas. There is still a strong need to enhance administrative capacity.

Progress has been made at a moderate pace in the field of *energy*. As regards alignment with the internal energy market *acquis* and the security of supplies and oil stocks, Cyprus has advanced only in a limited manner. Cyprus is strongly encouraged to ensure the progressive building up of oil stocks and the relevant authority according to the agreed timetable. Ongoing legislative work in order to align with the internal energy market *acquis* and to establish the oil stocks authority should be continued without delay, as should efforts to ensure the necessary oil stocks storage capacity.

Cyprus has continued the integration of the *environment* into other policies and has achieved a considerable alignment with the *acquis* in the various sectors of environmental and nature protection. However, measures need to be adopted in the important fields of air and water quality, industrial pollution control, chemicals, and genetically modified organisms. Particular attention should be paid to waste management and to enhancing administrative capacity. Investment needs to be secured in the medium term to ensure implementation of the environmental *acquis*.

Concerning *justice and home affairs* good progress in the fields of visa policy, asylum, the fight against organised crime and corruption can be reported. On asylum, alignment has been accelerated and an independent review authority has been established. Concerning the Schengen *acquis*, Cyprus is continuing its preparations by fully implementing the existing Schengen Action Plan and by developing the National information system. Cyprus has ratified various conventions with respect to data protection, the fight against terrorism, and proceeds from crime. In general, administrative capacity has still to be further strengthened in this area.

As regards *regional policy*, Cyprus has continued to make important progress in aligning with the *acquis* preparing for participation in structural instruments. Cyprus is also well advanced with respect to administrative structures.

Cyprus has achieved further progress in the field of *financial control*. Its Public Internal Financial Control system is well developed and international audit standards are largely met. Efforts should be undertaken as to strengthening the administrative capacity of the Treasury.

Cyprus has further strengthened its *administrative capacity*. Additional staff has been recruited in key areas and has been included in the Supplementary Budget for 2002, which is not yet approved. In important areas such as capital movement, competition, agriculture, taxation, customs, environment, and justice and home affairs enforcement structures have been reinforced. Close attention is required as regards the structures which are necessary to implement the *acquis* which will be applicable only upon accession, in particular as regards sound and efficient management of EC funds.

In the accession negotiations, 28 chapters have been provisionally closed. Cyprus is generally meeting the commitments it has made in the negotiations. However, delays have occurred with regard to the establishment of the fishing vessel register, and in the legal alignment as regards oil stocks and with the electricity Directive. These issues need to be addressed.

Bearing in mind the progress achieved since the 1998 Regular Report, the level of alignment that Cyprus has achieved at this point in time, and its track record in implementing the commitments it has made in the negotiations, the Commission considers that Cyprus will be able to assume the obligations of membership in accordance with the envisaged timeframe. In the period leading to accession, Cyprus needs to continue its preparations, in line with the commitments it has made in the accession negotiations.

C. Conclusion²⁹

The Commission has repeatedly concluded that Cyprus fulfils the political criteria. This was the conclusion of previous Regular Reports, and has been confirmed over the past year. Cyprus continues to fulfil the Copenhagen political criteria.

The state public administration has been considerably strengthened by the creation of new posts and the promotion of regular training.

Cyprus continues to respect human rights and freedoms. Cyprus has improved the procedure for the protection of refugees. It has abolished restrictions on the right to marry for Turkish Cypriots living in the south.

Cyprus is a functioning market economy and it should be able to cope with competitive pressure and market forces within the Union.

The first 1998 Regular Report already acknowledged the economic reform efforts undertaken by the Cypriot authorities to prepare for EU accession. Since then, the Cypriot authorities' commitment to the economic requirements of EU accession has been sustained.

Further improvements can be made to the functioning of markets by keeping to plans to liberalise the telecom, energy, air transport and postal services sectors. Adherence to the fiscal consolidation programme will contribute to reducing the current account deficit. Care must be taken to improve co-ordination of the supervision of co-operative financial institutions and banks.

Since the 1998 Regular Report, Cyprus has made substantial progress in the different areas of the *acquis*. The legislative alignment process has accelerated in recent years. Cyprus has continued to pay attention to implementation and enforcement structures.

Over the past year, Cyprus has further advanced with legislative alignment and has improved its position in relation to administrative capacity, in particular in the fields of social insurance, veterinary and phytosanitary inspections, pharmaceutical services, combating money laundering, ship inspection, inland revenue, planning, environmental services, consumer and health protection, and customs.

Overall, Cyprus has achieved a good degree of alignment with the *acquis* in most areas and is advanced towards reaching adequate administrative capacity to implement the *acquis* in a considerable number of fields, although further efforts remain to be made. Detailed plans have been agreed, in particular in the negotiations and in the Action Plan, to cover the remaining gaps.

There has been significant progress in the different areas of the internal market. As regards *free movement of goods* approximation has been completed in a number of sector-specific areas. The adoption of the framework legislation on the New and Global Approach principle, following an initial delay, has allowed substantial legislative

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progress and constituted an important step towards further alignment with the *acquis*. In the field of public procurement full alignment has not yet been achieved. Furthermore, efforts are still required for transposition of the *acquis* relating to the notification procedure, market surveillance and product safety. The newly established Company for Certification has reinforced the infrastructure for standardisation and certification, whereas Cyprus has to continue efforts to enhance its market surveillance systems. In the field of *free movement of persons* Cyprus has taken a major step by adopting the framework legislation on the recognition of professional qualifications. It has abolished inconsistencies as regards the co-ordination of social security systems and has reached a good level of administrative capacity. On *freedom to provide services* good progress can be reported in terms of harmonisation, in particular with legislation on insurance companies and banks, including offshore banks. Enhancement of administrative capacity should particularly continue as regards supervisory authorities in the field of financial services. The liberalisation of *capital movement* is on course to achieve full alignment by accession. Although the administrative capacity for combating money laundering has been further enhanced through the recruitment of additional personnel, Cyprus must continue sustained efforts in this domain.

As regards *company law*, Cyprus's legislative alignment with the *acquis* is at an advanced stage. With respect to intellectual and industrial property rights, further efforts are required to strengthen enforcement capacity in relation to border controls, combating piracy and counterfeiting. In the field of *competition* steady progress has been made in adopting anti-trust and state aid legislation. A substantial improvement in state-aid and in anti-trust enforcement is evident after years of standstill. The State aid monitoring authority and the fully independent authority for the protection of competition function well, but should be developed further.

Cyprus has reached a good level of legislative alignment in the field of *agriculture* and has taken significant steps as regards the establishment of the Common Market Organisations. However, the administrative capacity to implement and enforce the *acquis* needs to be further strengthened in this field. Due priority should be given to the preparation of the Integrated Administration and Control System. In the area of *fisheries*, legislation has been aligned to a reasonable extent. Administrative capacity is in place but needs to be further reinforced. Cyprus has continued its efforts to further reduce the number of fishing vessels under its flag, but its Fishing Vessel Register has not yet become fully operational. However, the relevant infrastructure for the establishment of the register has been introduced and the implementation mechanisms are under way.

The comprehensive tax reform, concerning both indirect and direct taxation, has moved Cyprus significantly forward in the field of *taxation*. Cyprus has also made important progress with developing the necessary administrative capacity and has reached an adequate level in this respect. Cyprus can also rely on a well-organised and well functioning *customs* administration. Further legislative alignment is needed concerning inward and outward processing, temporary importation, cultural goods, and procedural aspects. The adoption of the pending and outstanding legislation in this area is urgently required in order to achieve this alignment.

Cyprus needs to focus on full liberalisation of the telecommunications markets, speeding up the implementation of the *acquis*, and the establishment of the regulator's office

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Progress has been made at a moderate pace in the field of *energy*. As regards alignment with the internal energy market *acquis* and the security of supplies and oil stocks, Cyprus has advanced only in a limited manner. Cyprus is strongly encouraged to ensure the progressive building up of oil stocks and the relevant authority according to the agreed timetable. Ongoing legislative work in order to align with the internal energy market *acquis* and to establish the oil stocks authority should be continued without delay, as should efforts to ensure the necessary oil stocks storage capacity.

Cyprus has continued the integration of the *environment* into other policies and has achieved a considerable alignment with the *acquis* in the various sectors of environmental and nature protection. However, measures need to be adopted in the important fields of air and water quality, industrial pollution control, chemicals, and genetically modified organisms. Particular attention should be paid to waste management and to enhancing administrative capacity. Investment needs to be secured in the medium term to ensure implementation of the environmental *acquis*.

Concerning *justice and home affairs* good progress in the fields of visa policy, asylum, the fight against organised crime and corruption can be reported. On asylum, alignment has been accelerated and an independent review authority has been established. Concerning the Schengen *acquis*, Cyprus is continuing its preparations by fully implementing the existing Schengen Action Plan and by developing the National information system. Cyprus has ratified various conventions with respect to data protection, the fight against terrorism, and proceeds from crime. In general, administrative capacity has still to be further strengthened in this area.

As regards *regional policy*, Cyprus has continued to make important progress in aligning with the *acquis* preparing for participation in structural instruments. Cyprus is also well advanced with respect to administrative structures.

Cyprus has achieved further progress in the field of *financial control*. Its Public Internal Financial Control system is well developed and international audit standards are largely met. Efforts should be undertaken as to strengthening the administrative capacity of the Treasury.

Cyprus has further strengthened its *administrative capacity*. Additional staff has been recruited in key areas and has been included in the Supplementary Budget for 2002, which is not yet approved. In important areas such as capital movement, competition, agriculture, taxation, customs, environment, and justice and home affairs enforcement structures have been reinforced. Close attention is required as regards the structures

which are necessary to implement the *acquis* which will be applicable only upon accession, in particular as regards sound and efficient management of EC funds.

In the accession negotiations, 28 chapters have been provisionally closed. Cyprus is generally meeting the commitments it has made in the negotiations. However, delays have occurred with regard to the establishment of the fishing vessel register, and in the legal alignment as regards oil stocks and with the electricity Directive. These issues need to be addressed.

Bearing in mind the progress achieved since the 1998 Regular Report, the level of alignment that Cyprus has achieved at this point in time, and its track record in implementing the commitments it has made in the negotiations, the Commission considers that Cyprus will be able to assume the obligations of membership in accordance with the envisaged timeframe. In the period leading to accession, Cyprus needs to continue its preparations, in line with the commitments it has made in the accession negotiations.

D. Accession Partnership and Action Plan for strengthening administrative and judicial capacity: Global assessment

Cyprus's progress and overall state of preparation in respect of the Copenhagen criteria has been examined and conclusions drawn above. The present section assesses the extent to which the priorities of the Accession Partnership have been met and the measures foreseen under the Action Plan implemented according to schedule. It should be noted that both the Accession Partnership and the Action Plan have a time perspective of two years covering 2002 and 2003, providing for another 15 months for priorities to be met. Furthermore, much has already been achieved based on previous Accession Partnerships. The present one focuses on remaining specific and well-circumscribed topics identified as requiring more work to prepare Cyprus for membership. Therefore the analysis below only focuses on these specific topics and does not give an overall picture of the state of preparation of Cyprus in each domain.

The purpose of the Accession Partnership is to set out in a single framework:

- the priority areas for further work identified in the Commission's Regular Report;
- the financial means available to help candidate countries implement these priorities;
- the conditions which will apply to this assistance.

The Accession Partnerships are revised on a regular basis, to take account of progress made, and to allow new priorities to be set. The Council adopted a revised Accession Partnership for Cyprus in January 2002, based on a proposal from the Commission.

The revised Accession Partnership has served as the point of departure for the Commission and Cyprus to develop jointly an Action Plan to strengthen Cyprus's administrative and judicial capacity.

The purpose of the Action Plan is to identify jointly the next steps required for Cyprus to achieve an adequate level of administrative and judicial capacity by the time of accession, and ensure that all necessary measures in this regard are taken, providing Cyprus with targeted assistance in areas that are essential for the functioning of an enlarged Union.

Developing adequate administrative and judicial capacity for EU membership is a demanding and wide-ranging task, which requires detailed preparations in each and every domain covered by the Union's policies and legislation. In preparing individual Action Plans, the Commission has taken a comprehensive approach. All priorities from the revised Accession Partnerships, which relate to the development of administrative and judicial capacity, have been included in the Action Plans. Each of these priorities is treated separately in the Action Plans, and specific measures have been designed to address each of them.

In the following, progress in addressing each of these priorities is reported. For ease of reference and to avoid repetitions, wording from the *Accession Partnerships* is rendered in italics. As regards the measures foreseen by the Action Plan, implementation is checked against timetables and reported.

Political criteria

In January 2002, Mr Clerides and Mr Denktash started direct talks under the auspices of the United Nations to reach a political settlement (*see Part B. 2. Prospects for a political settlement*). Since Cyprus has continued its efforts to support a settlement under the auspices of the UN, therefore the Accession Partnership priority related to the political criteria has been met.

Economic criteria

Cyprus has accelerated liberalisation in some protected sectors of the economy. It has established a regulatory framework and appointed a regulator in the field of *telecommunications*. Energy prices have been made transparent to industrial end users by a law of November 2001. As regards *air transport*, the preparations to apply common rules for the allocation of slots at Community airports upon accession have been completed. The *conditions for enterprise and development, with particular attention to sectoral diversification and small and medium-sized enterprises (SMEs)*, have been improved by facilitating access to finance. Overall, the Accession Partnership priorities as regards the economic criteria have been met.

Ability to assume the obligations of membership

Chapter 1: Free movement of goods

As regards the *implementation of the New Approach Directives*, Cyprus has made good progress, with the enactment of the new Framework Law. Apart from this law, which regulates the horizontal issues of the New Approach Directives, some *product legislation* in this domain has been adopted. *Alignment in the field of pharmaceuticals for veterinary use, cosmetics and foodstuff* is ongoing. The Veterinary Drugs Council has been established and members of the Cosmetics Council have been appointed. The Action Plan foresees the adoption of a bill on the establishment of the Cyprus Organisation for Standards and Control of Quality (CYS) by the end of 1999, to *reinforce horizontal administrative infrastructure and implement capacity in the sectors covered by product specific legislation*. The CYS has been established (renamed "Cyprus Organisation for the Promotion of Quality" in the meantime), but the official determination of its responsibilities and of those of the new private organisation in this area has not taken place yet. The Action Plan also foresees full membership of CYS in CEN and CENELEC by accession. CYS has applied for membership of these bodies. As regards the *development and implementation of a market surveillance strategy*, progress is continuing slowly. The Action Plan states that the Department of Labour Inspection must be further enhanced through personnel recruitment in 2002. This still needs to be done. Continuous training of personnel of market surveillance authorities is going on as mentioned in the Action Plan, as is the training of State General Laboratory personnel. Further training of public inspectors, of personnel to be engaged in the implementation of harmonised legislation and of the staff of the Type Approval Authorities has also started as planned. The *systematic screening of legislation in the non-harmonised area to ensure that it is in compliance with Articles 28 to 30 of the Treaty* still needs to be completed. Overall, the Accession Partnership priorities in the area of free movement of goods have been partially met. Implementation of the measures under the Action Plan is on track.

Chapter 2: Free movement of persons

As regards *alignment of mutual recognition of professional qualifications and diplomas*, has made good progress with the enactment of the new Framework Law. Concerning the *co-ordination of social security systems*, Cyprus is progressing well. It has continued to apply its bilateral social security agreements with Member States, and a law amending the social insurance legislation was adopted in July 2002. The Action Plan foresees the development of the necessary *administrative structures* of the Department of Social Insurance through recruitment and training of personnel within 2002, but only a few actions have taken place. Extra budget resources for additional staff have still to be approved. Therefore, the Accession Partnership priorities in the field of free movement of persons have been partially met. Implementation of the Action Plan is on track.

Chapter 3: Freedom to provide services

Regarding *co-operative credit and savings societies (CCSSs)*, legislation incorporating the outstanding relevant provisions of the *acquis* on credit institutions is still to be completed. The Action Plan provides for the enhancement of the administrative capacity of the Department of Co-operative Development through the recruitment and training of additional staff and the technological upgrading of the electronic monitoring systems by January 2003. Preparations in this field have already started with the training of staff of the Department of Co-operative Development, and measures are underway for the full computerisation of all CCSSs as well as the upgrading of the electronic systems, as foreseen in the Action Plan. *Reinforcement of the supervision of financial services, which was in need of particularly urgent action*, has taken place. The responsible division in the Central Bank has the required administrative infrastructure and the necessary human resources with expertise in supervision. In the field of investment services and the securities market there is a further need to delineate the responsibilities and powers of the Securities and Exchange Commission and the Cyprus Stock Exchange. The Action Plan foresees the enhancement of the administrative capacity of the Insurance Companies Control Service through 2002 and 2003 and preparations are under way. Training on investment services was carried out in February-March 2002. Overall, the Accession Partnership priorities in the field of freedom to provide services have been met to a considerable extent. Implementation of the measures under the Action Plan is largely on track.

Chapter 4: Free movement of capital

Concerning compliance with the recommendations of the Financial Action Task Force, Cyprus continues to follow these recommendations. A new reporting system for balance-of-payments transactions has been implemented and the recruitment of eleven new staff in the unit for combating money laundering (MOKAS) has started. Since last year, banks are required without exception to ascertain the identity of all true beneficiaries of trust and nominee accounts. Thus, the Accession Partnership priority in the field of free movement of capital has been met to a large extent. Implementation of the Action Plan is on track.

Chapter 5: Company law

Enforcement of intellectual and industrial property rights is being strengthened. With regard to the strengthening of the law enforcement capacity to combat piracy and counterfeiting, *controls at border points* have been introduced, but must be intensified.

As regards the *fight against piracy and counterfeiting*, the Action Plan provides for enhancement of the administrative capacity of the judiciary and of all other enforcement bodies, which is on track, but remains an important task. The same is valid for targeted *training* of all services involved in the implementation and enforcement of IPR legislation, necessary for both copyright officials and for enforcement officials, including judges and prosecutors. An act amending copyright law was enacted in July 2002. Overall, the Accession Partnership priorities in the area of company law have been partially met. Implementation of the measures under the Action Plan is on track.

Chapter 6: Competition

In the field of State aid, *State aid legislation* and *existing aid* is brought into line with the *acquis*, including fiscal aid. A *regional aid map* was agreed, a *comprehensive State aid inventory and annual report* have been submitted. The *administrative capacity* was *strengthened*. The *enforcement of the rules in State aid* made good progress. Anti-trust measures are underway to further strengthen *the administrative capacity* of the Commission for the Protection of Competition, and Cyprus submitted an “Action plan for strengthening the administrative capacity of the Commission for the Protection of Competition” to the European Commission. It’s implementation requires further monitoring. As regards *enforcement of the rules in anti-trust and state aid*, some progress has been made. However, further efforts are needed in order to ensure the effective and deterrent application and enforcement of anti-trust rules, including sectors where the continuing existence of statutory monopolies and administrative orders regulating trade in certain goods prevents the normal application of competition rules. To *increase awareness of the rules among all market participants and aid grantors* seminars have been organised, articles and interviews have been published in the local press and the web-site of the Office of the Commissioner for Public Aid was activated. *Training of the judiciary* was increased, but needs to be further intensified. Overall, the Accession Partnership priorities in the field of competition have been partially met. Implementation of the measures under the Action Plan has been completed.

Chapter 7: Agriculture

In the Action Plan it is foreseen that the *setting up of the administrative structures for the Community-funded rural development programmes* must be completed by the end of 2002. Initial preparations have started and procedures to recruit 30 new officers to the Department of Agriculture are ongoing. Cyprus is partly behind schedule as regards the completion of the *preparations for the enforcement and practical application of the management mechanisms of the Common Agricultural Policy*, as the establishment and accreditation of the Paying Agency was provided for in the Action Plan by the end of 2001. The Minister of Agriculture, Natural Resources and the Environment has been appointed now as the responsible authority for the accreditation of the *Paying Agency* of Cyprus. A detailed timetable for making the Paying Agency operational by the time of accession was submitted. The Ministry of Agriculture has embarked on a coherent programme for the establishment and operation of an *Integrated Administration and Control System (IACS)*. *Implementation and enforcement of veterinary and phytosanitary and food safety legislation* has started, but needs to be completed. The Action Plan states that Cyprus has to complete the *preparations for bringing the status and operation of the current monopolies* in line with the *acquis* by January 2003, and the first preparations in this field are now under way. As regards *alignment of veterinary legislation*, the Action Plan provides that the Border Inspection Post (BIP) at Limassol port must be completed

by the end of 2002. As yet, it has neither facilities nor technical equipment. At the BIP at Larnaca Airport, the full range of facilities and equipment is not available. As regards *alignment of phytosanitary legislation*, good progress has been made. *Inspection arrangements* are not satisfactory and must be further *upgraded*. Overall, the Accession Partnership priorities in the area of agriculture have been partially met. Implementation of the measures under the Action Plan is progressing slowly.

Chapter 8: Fisheries

The process of *completion of the establishment of adequate administrative structures and equipment at central and regional level that can ensure the implementation of the Common Fisheries Policy* is ongoing. Three fisheries agreements and one convention have been ratified by the House of Representatives. The Inspectorate Service of the Department of Fisheries and Marine Research has appointed one additional inspector, bringing the number to 15. The Fisheries Department has revised its initial plans for the acquisition of a multi-purpose patrol vessel and has decided that such a vessel is not a high priority, at least for the time being. However the establishment of the *fishing vessel register* for the control of vessels fishing in the high seas, which Cyprus decided to finally implement, is behind schedule. Initially foreseen to be introduced by the end of 2001, it should now be established by the end of 2002. Cyprus continues its efforts to *reduce the number of fishing vessels* under its flag that operate in the high seas. It has decreased the number of vessels of over 24 metres from 104 in 1999 to about 30 today, thereby gradually reaching its target to reduce the number to 20 by accession. Overall, the Accession Partnership priorities in the area of fisheries have been partially met. Implementation of the measures under the Action Plan is partially on track.

Chapter 9: Transport policy

In view of the need for particularly urgent action regarding the alignment and implementation of maritime transport legislation, Cyprus has made some progress in legal alignment. With regard to the *enforcement of maritime safety standards*, as also required by the Action Plan, progress has been made through tighter controls. Cyprus has also achieved progress in terms of *further strengthening the administrative capacity of the Department of Merchant Shipping*, by creating 25 new posts for professional and clerical staff in the framework of the Action Plan. However, the full computerisation of the Department of Merchant Shipping needs to be completed. Cyprus should sustain its efforts to ensure that it will meet its objective of removing the *Cypriot flag* from the blacklist of the Paris Memorandum of Understanding. Cyprus *continued alignment in road transport*. As foreseen by the Action Plan, *administrative capacity in road transport* has been *strengthened* and has reached a fair level, except for the *transport of dangerous goods*, where the setting up of a new unit is lagging behind. *In aviation, particularly air safety*, the measures figuring in the Action Plan have been implemented. Overall, the Accession Partnership priorities in this area have been partially met. Implementation of the Action Plan is on track.

Chapter 10: Taxation

As regards *due alignment of the tax acquis, with particular attention to the VAT and excise duty regimes*, Cyprus has made significant progress, especially through the adoption of the tax reform concerning both indirect and direct taxation in July 2002. However, alignment still needs to be completed, notably concerning elimination of the

current protective import duties, so as to ensure equal taxation irrespective of origin. Legislation has been amended in order to eliminate potentially harmful tax measures and thus *comply with the Code of Conduct for Business Taxation*. The Commission's initial technical assessment of potentially harmful measures applied in Cyprus is ongoing. As regards *the strengthening of administrative capacity including control and enforcement procedures and administrative co-operation and mutual assistance*, the project for upgrading and updating the existing computerised VAT system has been completed, as stated in the Action Plan, in order to implement the new harmonised legislation approved by the House of Representatives. In the field of information technology, Cyprus is progressing. Progress has been made towards the establishment by the date of accession of a system of co-operation and *exchange of information with other national and EU Member States* with the implementation of the VAT Information Exchange System. Overall, the Accession Partnership priorities in the field of taxation have been met to a large extent. Implementation of the measures under the Action Plan is on track.

Chapter 12: Statistics

Cyprus has *improved the quality and coverage of statistics*. It has continued the measures already started as stated in the Action Plan: it has put in place the major economic classifications, has introduced a new survey on transport of goods by road and implemented the survey of goods and passengers by sea and a new system for the collection of harmonised statistics on "guest flows", "guest nights" and occupancy from collective accommodation establishments. Also, a population census was carried out and its results were published in January 2002. However, the implementation of the European System of Accounts (ESA 95) methodology has to be ensured. Cyprus has made good efforts *to ensure that adequate resources are available to further strengthen statistical capacities*, with the recruitment of new staff and an increase of the budget of the statistical service, while further enhancement of human and financial resources is already planned. Eurostat has performed a global assessment the conclusions of which are generally positive. Therefore, the Accession Partnership priorities in the area of statistics have been met to a large extent. Implementation of the measures under the Action Plan is on track.

Chapter 13: Social policy and employment

Cyprus has *continued to support the social partners' capacity building efforts*. They played an active role in the preparation of legislative measures for the transposition of the *acquis* and their capacity will be further enhanced through training. As regards *alignment of Community legislation* some directives still need to be transposed. The setting up of the Equality Committee is foreseen for the end of 2002 and, as stated in the Action Plan, an allocation has been made in the 2002 Budget for its administrative capacity. Enhancement of the administrative capacity of the Ministry of Labour and Social Insurance and the Labour Inspection Department is mentioned in the Action Plan but has not yet been approved by the House of Representatives.. Concerning *alignment and implementation of Community legislation on public health and adaptation of the national structures for surveillance and control of communicable diseases and health monitoring and information*, the measures foreseen in the Action Plan are either in preparation, as, for example, the Network for the Surveillance of Communicable Diseases and the Health Monitoring System, or on-going, such as the creation of a Public Health Laboratory. Regarding the *preparation of a national strategy with a view to future participation in the European strategy on social inclusion*, preparatory work for the implementation of

the measures in the Action Plan has started. Overall, the Accession Partnership priorities in this field have been met. Implementation of the measures under the Action Plan is on track.

Chapter 14: Energy

Cyprus has *continued the alignment* process regarding oil stocks, but the actual adoption of the relevant legislation is still pending. In accordance with its commitments Cyprus has *made progress in preparing*, according to its commitments, *the actual constitution of the stocks*. *The administrative structure* for oil stocks needs to be established, in accordance with the time schedule of the Action Plan. *Preparation for participation in the internal energy market, notably concerning the electricity directive, has continued*, but legislation still needs to be adopted, while the *establishment of a regulator and a common system operator for both transmission and distribution* remains to be done in accordance with the Action Plan. *Remaining price distortions* need to be removed. Concerning *the improvement of energy efficiency*, the measure planned in the Action Plan concerning the efficiency requirement for certain categories of products has been completed. Cyprus continued *enhancing the use of renewable energy* by implementing the measures foreseen in the Action Plan. Cyprus has accepted and adequately addressed all the *recommendations of the Council Report on Nuclear Safety in the Context of Enlargement*. Overall, the Accession Partnership priorities in the energy sector have only been met to a limited extent. There are delays in the implementation of the measures under the Action Plan.

Chapter 19: Telecommunications and information technologies

The new law on telecommunications and postal services has been adopted and *the introduction of a comprehensive regulatory framework* has been completed with the setting up of the National Regulatory Authority, the appointment of the Commissioner and Deputy Commissioner of Telecommunications and Postal Regulation and the Advisory Committee, as mentioned in the Action Plan. A regulation providing for the rapid recruitment of personnel for the NRA has been adopted and has allowed the recruitment of the 32 approved posts to start. Concerning the *monopoly for mobile voice telephony*, Cyprus has made progress but efforts have to be made to complete liberalisation and ensure fair competition. Therefore, the Accession Partnership priorities in this area have been partially met. Most measures under the Action Plan are on track.

Chapter 21: Regional policy and co-ordination of structural instruments

Cyprus has already started preparing the draft Single Programming Documents as required by the Structural Funds regulations and foreseen in the Action Plan. The overall division of responsibilities regarding the programming and implementation of Structural Funds and Cohesion Fund as in the Action Plan was approved by the Council of Ministers, including the detailed definition of the tasks of the Planning Bureau as the future Managing Authority for the Single Programming Documents and the co-ordinating authority for programming of the Structural Funds, the Paying Authority (Accounting and Financial Services Directorate of the Treasury), and the intermediate bodies. The Structural Funds Unit of the Planning Bureau is co-ordinating all remaining preparatory activities for the designation and the setting up of the implementation system. The *managing and paying authorities* have been defined through the designation of the Planning Bureau as the Managing Authority as mentioned in the Action Plan. Also a

small unit has been set up in the Planning Bureau for the co-ordination of all preparatory activities in relation to the Structural Funds. *In terms of recruitment and training* the Planning Bureau has accelerated its preparation process. The *required monitoring and evaluation systems for Structural Funds* have been set up, and the implementation plan for setting up a system for the management of Structural Cohesion Funds has been finalised and submitted. However, work on ensuring compliance with the *acquis requirements for ex-ante evaluation and for the collection and processing of the relevant statistical information and indicators* needs to continue. The *specific financial management and control procedures for future Structural and Cohesion Funds under the relevant Community regulations* has been further *aligned* through the establishment of an Internal Audit Board, but Cyprus must finalise the specific procedures for financial control, auditing, certification of expenses and correction of irregularities applicable to the Structural and Cohesion Funds. As regards the *development of the technical preparation of projects eligible for Structural and Cohesion Funds assistance*, there are delays in developing the new computerised financial information and management accounting system (FIMAS). Overall, the Accession Partnership priorities in the area of regional policy have been partially met. Implementation of the measures under the Action Plan is on track.

Chapter 22: Environment

Cyprus has *continued* with the *implementation of the acquis* in the field of waste management with the Law on Packaging and Packaging Waste, but further alignment in this field is necessary. As regards the *development of an implementation plan for the Water Framework Directive*, a monitoring programme has been put in operation as foreseen in the Action Plan. In the meantime, the Water Pollution Control Bill, which will transpose a number of water quality directives, has been passed. Also two sets of regulations, on the limitation of water pollution from asbestos and the management of sewage sludge, were approved. The *strengthening of the administrative and enforcement capacity* is ongoing. The Environment Service has been allocated 6 additional employees, and additional equipment for combating oil pollution accidents has been purchased. Cyprus has moved forward as regards *nature protection legislation*, as it has approved a scheme for the protection of specific areas of the environmentally sensitive Akamas peninsula from development. Overall, the Accession Partnership priorities in the field of environment have been partially met. Implementation of measures under the Action Plan is on track.

Chapter 24: Co-operation in the field of justice and home affairs

As regards *asylum, in particular the provision for manifestly unfounded claims*, Cyprus has introduced the necessary amendments to the Refugee Law incorporating the rights of refugees. *Enhancement of the administrative capacity* for the Refugee Authority, foreseen in the Action Plan, has been delayed. Cyprus has achieved further legislative alignment with the *common visa policy* but further steps are needed, in particular concerning visa-issuing capacity. Concerning the *implementation of the Schengen action plan and the preparation for participation in the Schengen information system*, efforts have been made but the modification of SIS II has resulted in delays of the Action Plan measures foreseen in this area. *Negotiations of a readmission agreement* with Syria are ongoing. A readmission agreement has been signed with Italy and proposals for negotiations have been sent to Romania and Egypt. The measures foreseen in the Action Plan concerning upgrading of border equipment are being implemented. As regards the *fight against*

money laundering, 11 posts were created for the Unit for Combating Money Laundering (MOKAS) of which 2 are for lawyers, 8 for investigators (accountants and financial analysts) and one for supporting/administrative staff. Recruitment started in July 2002. Cyprus has submitted its application for participation in the European Monitoring Centre for *Drugs and Drug Addiction* (EMCDDA) but this participation must be reinforced through the setting up of a National Focal Point and the development of a national drugs strategy. These measures, mentioned in the Action Plan, have not yet been completed. In the field of *data protection*, Cyprus has put in place the necessary structures and recruited the staff, thus implementing the measures under the Action Plan. Concerning *internal co-operation within the police*, a comprehensive study on the structure of the police has been completed and a multi-disciplinary team for inter-ministerial co-ordination *combating organised crime* has been set up. With a view to facilitating the negotiation of a *co-operation agreement with Europol*, Cyprus has translated into English the Law on Processing of Personal Data and forwarded it to Europol. Negotiations are on going. Cyprus has put in place legislation and the necessary administrative structures with regard to *the protection of the EC's financial interests*. In conclusion, the Accession Partnership priorities in this area have been partially met. Implementation of the Action Plan is on track.

Chapter 25: Customs union

Cyprus has *accelerated legislative harmonisation although not sufficiently and has strengthened institutional and administrative capacity*. The measures under the Action Plan, namely the development of a three-year business strategy, the reorganisation and restructuring of the Department of Customs and Excise, the recruitment of staff and the establishment of the Training and Development programme have been achieved. Cyprus *has continued the implementation of the IT strategy for the Cypriot customs administration*: the first phase of the computerisation of the Department of Customs and Excise has started and will be completed in October 2002, and the second and third phase are to be completed in March and September 2003 as foreseen in the Action Plan. Therefore, the Accession Partnership priorities in this area have been met. The implementation of the Action Plan is progressing as foreseen.

Chapter 26: External relations

There is no *international treaty or agreement incompatible with the acquis to be renegotiated or terminated by Cyprus's accession*. Cyprus has continued to inform the Union of negotiations aimed at the conclusion of new trade agreements with third countries. This Accession Partnership priority has been partially met.

Chapter 28: Financial control

As regards the *development of functional independence for internal controllers/auditors at both central and decentralised levels*, Cyprus has taken the necessary steps and put in place the necessary structures, and the measures under the Action Plan have been completed. *Work has been completed on an audit manual and on developing audit trails for the control of EC funds*. To *strengthen public financial control (PIFC) functions*, Cyprus is enhancing the administrative capacity of the Treasury through the continuous training of its staff and upgrading of the technology infrastructure, as foreseen in the Action Plan. The Accountant General is the contact point in relation to all PIFC issues. The Attorney General, as head of the Law Office, is the *single contact point for DG*

OLAF for the protection of the Communities' financial interests, and maintains good co-operation with OLAF. The measures under the Action Plan are being implemented. As regards the *fight against fraud*, the measures of the Action Plan concerning MOKAS have been partly implemented. It is being further reinforced. Cyprus has *continued its efforts to ensure the correct use, control, monitoring and evaluation of EC pre-accession funding* with the establishment of the necessary structures foreseen in the Action Plan and has continued its preparation for its accreditation to EDIS. Thus, the Accession Partnership priorities under this chapter have been met. The implementation of the Action Plan is progressing.

Annexes

***Human Rights Conventions ratified by the Candidate Countries,
15 September 2002***

<i>Adherence to following conventions and protocols</i>	BG	CY	CZ	EE	HU	LV	LT	MT	PL	RO	SK	SI	TK
ECHR (European Convention on Human Rights)	X	X	X	X	X	X	X	X	X	X	X	X	X
Protocol 1 (right of property)	X	X	X	X	X	X	X	X	X	X	X	X	X
Protocol 4 (freedom movement et al.)	X	X	X	X	X	X	X	X	X	X	X	X	O
Protocol 6 (death penalty)	X	X	X	X	X	X	X	X	X	X	X	X	O
Protocol 7 (ne bis in idem)	X	X	X	X	X	X	X	O	O	X	X	X	O
European Convention for the Prevention of Torture	X	X	X	X	X	X	X	X	X	X	X	X	X
European Social Charter	O	X	X	O	X	X	O	X	X	O	X	O	X
Revised European Social Charter	X	X	O	X	O	O	X	O	O	X	O	X	O
Framework Convention for National Minorities	X	X	X	X	X	O	X	X	X	X	X	X	O
ICCPR (International Covenant on Civil and Political Rights)	X	X	X	X	X	X	X	X	X	X	X	X	O
Optional Protocol to the ICCPR (right of individual communication)	X	X	X	X	X	X	X	X	X	X	X	X	O
Second Optional Protocol to ICCPR (death penalty)	X	X	O	O	X	O	X	X	O	X	X	X	O
ICESCR (International Covenant on Economic, Social and Cultural rights)	X	X	X	X	X	X	X	X	X	X	X	X	O
CAT (Convention against Torture)	X	X	X	X	X	X	X	X	X	X	X	X	X
CERD (Convention on the Elimination of All Forms of Racial Discrimination)	X	X	X	X	X	X	X	X	X	X	X	X	O
CEDAW (Convention on the Elimination of All Forms of Discrimination against Women)	X	X	X	X	X	X	X	X	X	X	X	X	X
Optional Protocol to the CEDAW	O	X	X	O	X	O	O	O	O	O	X	O	O
CRC (Convention on the Rights of the Child)	X	X	X	X	X	X	X	X	X	X	X	X	X

X = Convention ratified

O = Convention **NOT** ratified

BG=Bulgaria; CY=Cyprus; CZ=Czech Republic; EE=Estonia; HU=Hungary; LV=Latvia; LT=Lithuania; MT=Malta; PL=Poland; RO=Romania; SK= Slovak Republic; SV=Slovenia; T=Turkey

Statistical data

	1997	1998	1999	2000	2001
Basic data	in 1000				
Population (average)	743.5	748.8	753.2	757.0	762.3p
	in km²				
Total area	9,251	9,251	9,251	9,251	9,251
National accounts	Mio Cyprus Pound				
Gross domestic product at current prices	4,369	4,694	5,019	5,487	5,865
	1000 Mio ECU/euro				
Gross domestic product at current prices	7.5	8.1	8.7	9.6	10.2
	ECU/euro				
Gross domestic product per capita b) at current prices	11,500	12,300	13,000	14,300	15,100
	% change over the previous year				
Gross domestic product at constant prices (nat. currency)	2.4	5.0	4.6	5.1	4.0
Employment growth	-0.3	1.0	1.3	2.8	:
Labour productivity growth	2.7	3.9	3.2	2.2	:
	in Purchasing Power Standards				
Gross domestic product per capita at current prices	16,100	17,000	18,100	17,600	18,500
Structure of production	in % of Total Gross Value Added				
- Agriculture	4.3	4.4	4.2	3.7	3.9
- Industry (excluding construction)	14.2	13.8	13.2	13.1	12.4
- Construction	8.4	8.0	7.7	7.1	7.1
- Services	73.1	73.8	74.9	76.1	76.6
Structure of expenditure	as % of Gross Domestic Product				
- Final consumption expenditure	84.8	86.7	83.4	85.1	86.1
- household and NPISH	66.0	67.5	65.7	:	:
- general government	18.8	19.3	17.7	:	:
- Gross fixed capital formation	18.1	17.2	16.1	:	:
- Stock variation	1.1	1.1	1.6	:	:
- Exports of goods and services	47.1	43.6	44.6	46.5	46.9
- Imports of goods and services	52.1	51.1	47.6	52.3	51.8
Inflation rate	% change over the previous year				
Consumer price index c)	3.3	2.3	1.1	4.9	2.0
Balance of payments	in Mio ECU				
- Current account	-298.5	-540.9	-203.9	-495.0	-457pf
- Trade balance	-1,827	-2,175	-2,166	-2,826	:
<i>Exports of goods</i>	1,099	955	938	1,031	:
<i>Imports of goods</i>	2,926	3,130	3,104	3,857	:
- Net services	1,516	1,634	1,916	2,212	:
- Net income	-10	-26	-36	-18	:
- Net current transfers	23	26	82	136	:
<i>-of which: government transfers</i>	15	23	82	139	:
- FDI (net) inflows	67	62	114	174	182pf
Public finance	in % of Gross Domestic Product				
General government deficit/surplus	:	:	:	:	:
General government debt	:	:	:	:	:
Financial indicators	in % of Gross Domestic Product				
Gross foreign debt of the whole economy d)	147.0	60.2	73.4	74.9	:
	as % of exports				
Gross foreign debt of the whole economy d)	312.4	138.2	164.5	162.4	:

	1000 Mio ECU /euro				
Monetary aggregates					
- M1	1.2	1.3	1.8	1.9	1.9
- M2	8.1	8.8	10.2	11.1	12.6
- M3	:	:	:	:	:
Total credit	9.9	11.1	12.5	14.3	16.5
Average short-term interest rates	% per annum				
- Day-to-day money rate	4.7	4.8	5.2	6.0	4.9
- Lending rate	8.1	8.0	8.0	8.0	7.5
- Deposit rate	6.3	6.5	6.5	6.5	4.8
ECU/EUR exchange rates	(1ECU/euro=Cyprus Pound)				
- Average of period	0.583	0.577	0.579	0.574	0.576
- End of period	0.580	0.582	0.577	0.574	0.575
	1995=100				
- Effective exchange rate index	102.8	108.3	106.0	102.2	104.9
Reserve assets	Mio ECU/euro				
-Reserve assets (including gold)	1,385	1,299	1,959	2,009	2,711
-Reserve assets (excluding gold)	1,263	1,184	1,829	1,873	2,565

	Mio ECU/euro				
External trade					
Trade balance	-2,141	-2,330	-2,422	-2,990	-3,289
Exports	403	407	393	440	491
Imports	2,544	2,737	2,815	3,430	3,780
	previous year=100				
Terms of trade	:	:	:	:	:
	as % of total				
Exports with EU-15	50.2	54.3	53.7	51.5	49.0
Imports with EU-15	56.3	61.9	57.3	55.9	55.5

	per 1000 of population				
Demography					
Natural growth rate	6.3	5.2	5.2	4.6	4.3p
Net migration rate (including corrections)	0.7	2.0	-0.8	1.1	4.1p
	per 1000 live-births				
Infant mortality rate	8.0	7.0	6.0	5.6	5.0p
Life expectancy :	at birth				
Males:	75.0	:	75.3	:	:
Females:	80.0	:	80.4	:	:

	% of population				
Labour market (Labour Force Survey) e)					
Economic activity rate (15 - 64)	:	:	68.3	69.0	70.8
Employment rate (15-64), total	:	:	64.2	65.5	67.9
Employment rate (15-64), male	:	:	78.7	78.9	79.7
Employment rate (15-64), female	:	:	50.2	52.5	56.5
	in % of total				
Average employment by NACE branches					
- Agriculture and forestry	9.2	9.1	4.7	5.4	4.9
- Industry (excluding construction)	15.0	14.5	14.6	14.1	14.0
- Construction	9.4	9.1	10.0	10.0	10.0
- Services	66.4	67.3	70.7	70.5	71.1
	% of labour force				
Unemployment rate, total	3.4	3.4	5.9	4.9	4.0
Unemployment rate, males	2.7	2.9	4.5	3.2	2.7
Unemployment rate, females	4.5	4.2	7.9	7.4	5.8
Unemployment rate of persons < 25 years	:	:	11.9	10.5	8.4
	as % of all unemployed				
Long-term unemployment share	7.9	8.0	22.1	25.8	21.9

Infrastructure	in km per 1000 km²				
Railway network	0	0	0	0	0
	km				
Length of motorways	199	204	216	240	257

Industry and agriculture	previous year=100				
Industrial production volume indices	99.8	102.6	102.1	104.5	99.7
Gross agricultural production volume indices	88.3	109.4	107.4	91.5	106.4p

Standard of living	per 1000 inhabitants				
Number of cars	359.0	377.0	387.0	400.0	416.0
Main telephone lines	589.8	612.8	637.9	657.7	644.9
Number of subscriptions to cellular mobile services	140.5	176.3	228.1	326.3	466.1
Number of Internet subscriptions	24.6	44.4	55.4	89.1	99.5

p=provisional figures

- a) Data provided refer to the Government controlled area only, with the exception of data on total area, population and the various demographic indicators which refer to the whole of Cyprus. indicators expressed in per capita were calculated on the basis of the mid-year population in the Government controlled area: 1996: 648,1; 1997: 654,5; 1998: 660,4; 1999: 664,8; 2000: 669,1 and 2001: 674,5 (P).
- b) Figures have been calculated using the population figures from National Accounts, which may differ from those used in demographic statistics.
- c) Changes in Methodology: PROXY HICP since 1998 (see methodological notes).
- d) Series break in 1998: adjusted for offshore financial activity.
- e) Data for the years 1999 - 2001 based on largely EU-harmonised LFS data collected in the second quarter of each year (April - June). Data for the years 1997 - 1998 are compiled from a number of administrative sources. Data on unemployment refer to the registered unemployed. Data on employment are calculated on a FTE basis.
- f) Source: Website of the National Bank

Methodological Notes

Inflation rate

As part of the preparations for the common currency the EU Member States (MSs) have designed a new *consumer price index* in order to comply with the obligations of the EU Treaty. The aim was to produce CPIs comparable between Member States. The main task was to harmonise methodologies and coverage. The result was the Harmonised Index of Consumer Prices (HICP). A similar exercise has been started with Candidate Countries (CC). In respect to enlargement, it is equally important that their economic performance is assessed on the basis of comparable indices. Some progress has already been made towards adapting the new rules. Since January 1999 CCs report monthly to Eurostat so-called proxy HICPs that are based on national CPIs but adapted to the HICP coverage. They are not yet fully compliant with the HICPs of the MSs. In the table, the proxy HICPs are back-calculated to 1996 (rates from 1997).

Finance

Public finance: The government deficit and debt statistics of the Candidate Countries are provisional, in the sense that they do not yet fully comply with EU methodological requirements. Broadly speaking, the general government deficit / surplus refers to the national accounts concept of consolidated general government net borrowing / net lending of ESA95. General government debt is defined as consolidated gross debt at end-year nominal value. The series for Cyprus are presently available from 1998 only; the 1996-97 data are an approximation derived from the IMF's GFS methodology.

Gross foreign debt is of the whole economy, covering both short- and long-term, but excluding equity investment and money market instruments. The source for stock of outstanding debt is OECD, while the source of GDP is Eurostat. For the ratio of gross foreign debt to exports, the national accounts definition of exports of goods and services is used (source: Eurostat). The data for 2000 are Eurostat estimates, based on joint OECD/IMF/BIS/World Bank series.

Monetary aggregates are end-year stock data, as reported to Eurostat. Generally, M1 means notes and coin in circulation plus bank sight deposits. M2 means M1 plus savings deposits plus other short-term claims on banks. M3 means M2 plus certain placements in a less liquid or longer-term form. Not all countries produce an M3 series. Total credit means loans by resident monetary financial institutions (MFIs) to non-MFI residents.

Interest rates: Annual average rates based on monthly series reported to Eurostat. Lending rates refer to bank lending to enterprises for over 1 year. Deposit rates refer to bank deposits with an agreed maturity of up to one year. Day-to-day money rates are overnight interbank rates.

Exchange rates: ECU exchange rates are those that were officially notified until 1 January 1999, when the ECU was replaced by the euro. Euro exchange rates are reference rates of the European Central Bank. The effective exchange rate index (nominal), as reported to Eurostat, is weighted by major trading partners.

Reserve assets are end-year stock data, as reported to Eurostat. They are defined as the sum of central bank holdings of gold, foreign exchange, SDRs, reserve position in the IMF, and other claims on non-residents. Gold is valued at end-year market price.

External trade

Imports and exports (current prices). The data are based upon the special trade system, according to which, external trade comprises goods crossing the customs border of the country. Trade data excludes direct re-exports, trade in services and trade with customs free zones as well as licences, know-how and patents. Value of external trade turnover includes the market value of the goods and the additional costs (freight, insurance etc.). *Trade Classification*. Trade in goods is recorded using the commodity classification according to the Combined Nomenclature (CN).

The term FOB means that all costs incurred in transport up to the customs frontier are charged to the seller. The term CIF means that the purchaser pays the additional costs. Imports are recorded on CIF basis, exports on FOB basis.

Imports and exports with EU-15. Data declared by the Republic of Cyprus.

Demography

Net migration rate. Crude rate of net migration for year X, is:

$\{\text{population as at 31 December (X)} - \text{population as at 1 January (X)} + \text{Deaths (X)} - \text{Births (X)}\} / \text{average population (X)}$. This assumes that any change in population not attributable to births and deaths is attributable to migration.

Labour force

Data for the years 1997 - 1998 are compiled from a number of administrative sources.

Data for the years 1999 - 2001 refer to national LFS data collected in the second quarter of each year (April - June).

Basic concepts and definitions (LFS): All definitions apply to persons aged 15 years and over, living in private households. The concepts and definitions used in the survey follow the guidelines of the International Labour Organisation.

Persons in employment were those who during the reference week did any work for pay or profit for at least one hour, or were not working but had jobs from which they were temporarily absent. Family workers are included.

As from 2001 (Commission Regulation (EC) No 1897/2000 of 7 September 2000), *unemployed persons* comprise persons aged 15 to 74 who were:

- (a) without work during the reference week, i.e. neither had a job nor were at work (for one hour or more) in paid employment or self-employment;
- (b) currently available for work, i.e. were available for paid employment or self-employment before the end of the two weeks following the reference week;

(c) actively seeking work, i.e. had taken specific steps in the four weeks period ending with the reference week to seek paid employment or self-employment or who found a job to start later, i.e. within a period of at most three months.

Comparability with results prior to 2001: unemployment results used to refer to persons aged 15 and more. Persons who found a job to start later used to be considered as unemployed with the unique condition to have no job in the reference week. Data for the years 1997 - 1998 are compiled from unemployment registers.

Duration of unemployment is defined as:

(a) the duration of search for a job, or

(b) the length of the period since the last job was held (if this period is shorter than the duration of search for a job).

The active population is defined as the sum of persons in employment and unemployed persons.

Inactive persons are those who are not classified as persons in employment nor as unemployed persons.

Employment rates represent employed persons aged 15-64 as a percentage of the same age population.

Unemployment rates represent unemployed persons as a percentage of the active population aged 15 years and more.

Economic activity rates represent the active population aged 15-64 as a percentage of the population of the same age.

Data on average employment by NACE branches are calculated on a Full Time Equivalent basis.

Infrastructure

Railway network. All railways in a given area. This does not include stretches of road or water even if rolling stock should be conveyed over such routes; e.g. by wagon-carrying trailers or ferries. Lines solely used for tourist purposes during the season are excluded as are railways constructed solely to serve mines; forests or other industrial or agricultural undertakings and which are not open to public traffic. The data considers the construction length of railways.

Length of motorway. Road, specially designed and built for motor traffic, which does not serve properties bordering on it, and which:

(a) is provided, except at special points or temporarily, with separate carriageways for the two directions of traffic, separated from each other, either by a dividing strip not intended for traffic, or exceptionally by other means;

(b) does not cross at level with any road, railway or tramway track, or footpath;

(c) is specially sign-posted as a motorway and is reserved for specific categories of road motor vehicles.

Entry and exit lanes of motorways are included irrespectively of the location of the signposts. Urban motorways are also included.

Industry and agriculture

Industrial production volume indices. Industrial production covers mining and quarrying, manufacturing and electricity, gas, steam and water supply (according to the NACE Rev.1 Classification, Sections C, D and E).

Gross agricultural production volume indices. Gross agricultural production volume indices are calculated in constant prices of 1995.

Standard of living

Number of cars. Passenger car: road motor vehicle, other than a motor cycle, intended for the carriage of passengers and designed to seat no more than nine persons (including the driver).

The term "passenger car" therefore covers all private saloon cars, taxis and hired passenger cars, learner's vehicles and invalid carriages, provided that they have less than ten seats. This category does not include pick-ups.

Telephone subscribers. The number of telephone subscribers per 1000 inhabitants refers to the number of direct exchange lines (fixed telephone only) and does not include mobile phone subscribers.

Internet connections. The number of internet connections per 1000 inhabitants refers to the number of internet subscribers to all internet access service providers in Cyprus.

Sources

Total area, external trade, labour market, infrastructure, demography, industry and agriculture, standard of living (including Internet connections): National sources.

National accounts, inflation rate, balance of payment, public finance, finance: Eurostat.