



The Phare Programme

Annual Report 1999

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Message from the Commissioner

This 1999 Annual Report covers a key period of transition in the development both of the enlargement process and the Phare programme, its main financial instrument.

The Phare programme is one of the three pre-accession instruments financed by the European Communities to assist the applicant countries of central Europe in their preparations for joining the European Union. Phare's total "pre-accession" focus was put in place in 1997 in response to the Luxembourg European Council's launching of the present enlargement process. Phare funds now focus entirely on the pre-accession priorities highlighted in each country's Accession Partnership.

These basic orientations were adjusted in 1999 to reflect the coming on stream of Sapard in agriculture and rural development and of ISPA in transport and environment infrastructure. The principal adjustment was to redirect Phare's liberated funds towards tackling the issue of economic and social cohesion.

The 1997 reforms – especially those setting up new implementation structures – were fundamental and took some twelve to eighteen months to complete, making 1999 effectively the first year of operation of the reformed Phare programme. The overall results already indicate that the reforms were well judged:

- ? Phare programming has been fully re-oriented towards the accession objectives in the Accession Partnership and National Programme for the Adoption of the Acquis, as redefined annually by the Regular Reports and negotiations.
- ? Twinning is operational with 124 Twinning projects involving member states' civil servants in place advising their counterparts in national administrations on priority acquis issues.
- ? The new management structures are now operational in all ten candidate countries based on National Funds, Central Financing and Contracting Units and Implementing Agencies. More responsibility has been deconcentrated to Commission Delegations.
- ? The first Phare programme focusing on promoting economic and social cohesion was financed in 2000 on the basis of draft national development plans written by the countries in 1999.

I commend this Annual Report as a record of the events and achievements of the 1999 Phare programme and hope that it would serve as a useful documentation of the Programme's essential role in preparing the Candidate Countries for membership.

GÜNTER VERHEUGEN

Phare in 1999

The year in review

In addition to the ten candidate countries of Eastern and Central Europe that benefit from the Phare programme, Albania, Bosnia and FYROM, who are not candidate countries, received support from Phare in 1999. Malta, Cyprus and Turkey are also candidates but are not mentioned in this report due to the fact that they are not beneficiaries of Phare support.

Enlargement - priority activities and objectives

At its meeting in Berlin on 24-25 March 1999, the European Council confirmed that enlargement is a historic priority for the European Union, and that the accession negotiations would continue "each in accordance with its own rhythm and as rapidly as possible." In the framework of Agenda 2000, the Berlin European Council adopted new financial perspectives for the Union in the context of enlargement, covering the period 2000-2006. These new perspectives make financial provision both for pre-accession expenditure and for the first new Member States to join the EU between 2002-06. In concrete terms, up to € 3.12 billion annually have been allocated for pre-accession expenditure, and a total of up to € 58 billion has been set aside to finance Structural Funds programmes, internal policies, administration and agriculture in the newly acceding states.

In December 1999, on the basis of the Regular Reports presented by the European Commission on the progress towards accession of the central and eastern European candidate countries, the Helsinki European Council decided to open accession negotiations with Bulgaria, Latvia, Lithuania, Romania and Slovakia.

Considerable progress was made in the accession negotiations which had already begun with the Czech Republic, Estonia, Hungary, Poland and Slovenia: two-thirds of the 31 chapters had been opened to negotiation by the end of 1999 and a third provisionally concluded. In the context of the pre-accession strategy, the Council adopted revised Accession Partnerships for the negotiating countries and regulations on the pre-accession structural and agricultural instruments and on coordination between the different instruments and the Phare Programme.

European conference

In accordance with the conclusions of the Vienna European Council, a meeting of the foreign ministers of the 15 EU Member States and the candidate countries took place in Brussels on 19 July 1999. The meeting focused on the fight against transitional organised crime and the situation in the western Balkans. In December, the Council adopted a report on the work of the conference and of other fora engaged in similar work which it presented to the Helsinki European Council, which concluded that the conference's future would be reviewed in the light of developments and of decisions taken on the accession process.

Regular Reports

Following the Regular Reports on the progress towards accession of the candidate countries adopted by the European Commission in 1998, the European Parliament adopted a number of resolutions on 15 April 1999 on five reports concerning the countries with which negotiations had already started (the Czech Republic, Estonia, Hungary, Poland and Slovenia).

On 13 October, the Commission adopted its 1999 Regular Reports and a composite paper on the progress towards accession of the candidate countries. On the basis of a detailed analysis of the progress towards accession made by each of the countries, the Commission concluded in these reports that all central and eastern European countries met the political criteria laid down by the Copenhagen European Council, but that none fully met the economic criteria. It also noted that progress in the adoption of the *acquis* varied between candidate countries. Based on these reports, the Commission recommended opening negotiations with Latvia, Lithuania and Slovakia and, conditionally, with Bulgaria and Romania. It also recommended that the negotiations be conducted in accordance with the principle of differentiation, thereby taking account of the progress achieved, and that steps be taken to decide from 2002 on the accession of candidates that fulfil all the necessary criteria.

Further to the above recommendations, the Helsinki European Council decided to convene bilateral intergovernmental conferences in February 2000 with a view to opening negotiations with Bulgaria, Latvia, Lithuania, Romania and Slovakia, stressing that each candidate country would be judged on its own merits in the negotiations. Finally, the European Council made a political commitment to make every effort to complete the intergovernmental conference in time so that the European Union (EU) would be in a position to welcome new Member States from the end of 2002, as soon as they had demonstrated their ability to assume the obligations of membership and once the negotiating process had been successfully completed.

Accession negotiations

The process of screening the Community *acquis* with the five central and eastern European countries with which negotiations had been formally opened in March 1998 (the Czech Republic, Estonia, Hungary, Poland and Slovenia), as well as with Bulgaria, Latvia, Lithuania, Romania and Slovakia, was concluded in autumn 1999 except for the chapter on agriculture.

In the accession negotiations with the Czech Republic, Estonia, Hungary, Poland and Slovenia, two more ministerial conferences were held, one on 22 June in Luxembourg, the other on 7 December in Brussels. Each of these conferences was preceded by two preparatory conferences at deputy level (on 19 April and 19 May and on 30 September and 4 November). Sixteen new chapters were opened to negotiations at these conferences, bringing to 23 the total negotiated since the beginning of the process in 1998.

Pre-accession strategy

On 13 October, the Commission proposed the revision of the Accession Partnerships drawn up in 1998 for the candidate countries of Central and Eastern Europe to take account of the progress they had achieved. On this basis, detailed Accession Partnerships for each country were adopted by the Commission. Each country's Accession partnership sets out clear priorities. It also highlights the main instruments and financial resources available, all of which should be maximised to target the objectives effectively. The Accession Partnerships are therefore, the single programming framework for European Community assistance.

On 26 May, the Commission adopted a communication on countering racism, xenophobia and anti-Semitism in the candidate countries. The Council adopted conclusions on 26 October concerning cooperation with the candidate countries in the public health field. In response to communications from the Commission on those subjects, the European Parliament adopted resolutions on nuclear-sector-related activities for the central and eastern European candidate countries on 11 March and on the pre-accession strategy in the environmental field, an area it considered a priority, on 15 April. In December, the European Council also recalled the importance of high standards of nuclear safety in central and Eastern Europe. The Economic and Social Committee adopted a report on 7 July on the employment and social situation in the candidate countries and, on 8 December, an own-initiative opinion on the situation in Poland.

Europe Agreements and other agreements

The Europe Agreement with Slovenia entered into force on 1 February, replacing the 1993 Cooperation Agreement. The new agreement will permit more extensive cooperation, thereby facilitating implementation of the pre-accession strategy for Slovenia.

The protocols adapting the Europe Agreements to take account of the accession of Austria, Finland and Sweden to the EU and the results of the Uruguay Round entered into force on 1 January for Hungary, Latvia and Romania and on 1 September for Estonia and Lithuania. The Council concluded a similar protocol with Bulgaria on 9 March. It was signed on 25 March.

The Association Councils set up by the Europe Agreements adopted decisions on competition rules (Estonia, Latvia, Lithuania, Romania), rules of origin (Hungary, Lithuania, Poland, Slovakia) and a double-checking system for trade in ECSC products (Poland and Slovakia). They adopted further decisions concerning the participation of the candidate countries in Community programmes, more specifically allowing the 10 central and east European countries to participate in the Fifth Research and Technological Development Framework programme; Lithuania and Romania in the Raphael programme on protecting cultural heritage; Bulgaria and Slovenia in education and training programmes; the Czech Republic, Lithuania, Romania and Slovenia in programmes in the public health field and on equal opportunities; Bulgaria, Hungary, Lithuania and Romania in the SAVE II programme to promote energy efficiency; and Romania and Slovenia in programmes supporting small businesses. The Commission set out its approach on the candidate countries'

participation in Community programmes, agencies and committees in a communication on 20 December.

Adoption of ISPA, SAPARD and the Coordination Regulation

As part of Agenda 2000, the Council adopted three regulations on 21 June establishing the framework of aid to the candidate countries of central and eastern Europe for the period 2000-2006. Regulation (EC) No 1267/1999, established a pre-accession structural instrument to provide aid for improving the environment and transport infrastructure (ISPA). Regulation (EC) No 1268/1999, established a pre-accession instrument to support agricultural and rural development (SAPARD). Regulation (EC) No 1266/1999, is designed to co-ordinate and ensure the consistency of aid operations under the above two instruments and the Phare Programme.

Implementation of the new Phare guidelines

General overview

The European Commission has increasingly transferred responsibility for the management and implementation of Phare programmes to the authorities in the candidate countries of eastern and central Europe. This is part of the process of helping them to prepare for accession to the European Union (EU).

In 1999, candidate countries had to implement simultaneously both 'old Phare' programmes decided before 1998 and managed through PMUs and 'new-Phare' programmes decided after 1998. The 'new-Phare' programmes follow on from the 1998 new orientations for Phare¹. They reflect the accession-driven approach and are focused solely on institution building and investment in the *acquis*. They are managed through the new structure of a National Fund and a limited number of Implementing Agencies in each country. A key role is played by the Central Finance and Contracting Unit which manages all institution building programmes (as well as some investment activities co-financed by Phare). The other Implementing Agencies are intended to develop into the administrative structures that will be needed to implement the Structural Funds after accession.

The new implementation mechanisms reflect the lessons learned from implementation of the Phare Programme in previous years and, in particular, the need to ensure that a limited number of 'centres of excellence' be responsible for handling EU funds. This is an essential precondition for full transfer of responsibility for tendering and contracting from the Commission to the candidate country (extended decentralisation).

The accession-driven focus that underpins the new orientations of Phare inevitably involves an increasing emphasis on national programmes designed to address the specific weaknesses identified in the Regular Reports that the Commission prepares on each candidate country. The corollary is a reduction in the importance of multi-country programmes. Previously these were useful in raising awareness of issues - especially those relating to the *acquis* - of common interest to several candidate countries. The need now is to help each country prepare itself to implement the *acquis*.

In the course of 1999, revised guidelines were developed for Phare and were approved by the Commission (SEC (1999) 1596 of 13 October). These guidelines build on the changes decided in 1998. They take account of the new ISPA and SAPARD regulations that take effect from 2000. (Henceforth major transports and environment projects will be financed from ISPA while agricultural and rural development will be financed by SAPARD. Phare cannot therefore finance projects in these areas.) The new guidelines also emphasise the need to use the Phare Programme to help the candidate countries prepare to benefit from the Structural Funds after accession (economic and social cohesion).

¹ The 'Guidelines for Phare programme implementation in candidate countries, 1998-1999' were adopted in June 1998 and cover the Phare budgets for 1998 and 1999.

In addition, the Commission has revised and strengthened the internal arrangements within Delegations for overseeing the tendering and contracting carried out by the authorities of the candidate countries. This has enabled the Commission to increase the upper limit for tender dossiers and contracts to be endorsed by the Delegation locally from € 500,000 to € 5 million.

Financial and technical assistance

In 1999, aid to the candidate countries of central and eastern Europe under Phare was provided in accordance with the new guidelines decided in 1998 (as revised to take account of the new financial instruments), which shift the whole focus of the programme towards preparing for accession. Approximately 70 per cent of the aid went on investments designed to improve the regulatory framework and economic and social cohesion, thereby facilitating adoption of the *acquis*, and 30 per cent on institution building, the main instrument of which was twinning (secondment of experts from Member State governments and agencies to the candidate countries to help on specific projects).

In 1998 and 1999, twinning arrangements were made in four sectors identified as short-term priorities in the Accession Partnerships: agriculture, environment, finance and justice and home affairs. Examples of twinning arrangements include projects on reforming the veterinary control administration in Bulgaria, improving the function and enhancing the independence of the judiciary in the Czech Republic and modernising Hungary's tax system. Steps were taken to speed up implementation of the programme by decentralising operations to the Commission's Delegations in the candidate countries.

The total Phare budget for 1999 (which also covers Albania, Bosnia and Herzegovina and the Former Yugoslav Republic of Macedonia) amounted to € 1,527 million.

The operations financed were

- national programmes: € 782 million, of which
 - Albania: € 46 million
 - Bulgaria: € 51 million
 - Czech Republic: € 21 million
 - Estonia: € 8 million
 - Hungary: € 103 million
 - Latvia: € 16 million
 - Lithuania: € 30 million
 - Poland: € 231 million
 - Romania: € 167 million
 - Slovakia: € 78 million
 - Slovenia: € 31 million
- cross-border cooperation: € 180 million
- regional and horizontal programmes: € 461 million
- rehabilitation of former Yugoslavia (excluding Kosovo reconstruction aid): € 42 million
- other: € 62 million.

Phare cross-border cooperation

The new Phare Cross-border Cooperation Regulation (CBC), adopted by the Commission on 18 December 1998², has introduced a number of important changes for programming and implementing Phare CBC, in comparison with the 1994-1998 period. These changes have taken account of the evaluation of the programme, which was made in 1998, and aim at better integrating the programme in the central and eastern European countries' overall regional development strategies. Together with the Phare reform of 1997, they ensure a more balanced and efficient programme, which is also better aligned with the main Phare Programme and Interreg.

The main changes introduced by the new regulation include

- the geographical extension of the programme, whereby, in addition to the border regions adjacent to the EU, those between the candidate countries themselves also become eligible
- the preparation by a joint committee of a single joint programming document, covering both sides of the border and drawn up in a multi-annual perspective
- specific provisions concerning Joint Small Project Funds, allowing the selection and implementation of small projects at the local level in a certain number of areas.

The budgetary appropriation in 1999 was € 180 million, as it was in 1998. However, following the eligibility of borders between candidate countries, and in compliance with the budgetary comment providing that up to one third of the appropriation had to be earmarked for those borders, allocations for borders with the EU were reduced correspondingly. Of the total budgetary appropriation, € 118 million was allocated to borders between candidate countries and the EU, 34 million to borders between candidate countries, € 21 million to borders between non-candidate countries and the EU, and € 7 million³ to the candidate countries bordering the Baltic Sea.

The Commission invited the countries to start programming Phare CBC with their neighbours in January 1999, and the full amount of € 180 million was approved by the Phare Management Committee and committed in time. Projects were jointly selected on the basis of priorities established in the Accession Partnerships and in the 1995-1999 Phare CBC Multi-annual Indicative Programmes and Interreg II Operational programmes. Most projects related to infrastructural development in the fields of transport and the environment. The minimum project size of € 2 million was applied, although in a flexible manner; in several cases, projects for less than € 2 million were accepted, provided strong cross-border impact was shown.

On most borders, including newly eligible borders between candidate countries, Small Project Funds continued to operate, or were established, using between 10 and 20 per cent of appropriations. This allowed regional and local actors to become increasingly involved in the programme.

² Commission Regulation (EC) N° 2760/98, OJ L345 of 19.12.1998.

³ This amount was transferred to budget article B7 537 'Special Action for the Baltic Sea region' and added to the € 5 million on that line earmarked for the candidate countries concerned.

At the invitation of the Commission, candidate countries and their neighbours also started actively preparing data with a view to preparing joint programming documents for the 2000-2006 period.

Multi-beneficiary programmes

▪ Lien and Partnership programmes

A substantial delay in the signature of contracts under the 1997 Phare LIEN and Partnership programmes was incurred due to the discussion between the European institutions regarding the possible role of an administrative and financial technical assistance office in their implementation. Co-financing agreements eventually concluded at the end of the year are based on the new standard grant contract developed by the Common Service for External Relations. The contract reduces the administrative burden on grant beneficiaries and combines more flexibility in the use of funds with the need for annual financial audits for projects with grant funding exceeding € 100,000.

The November meeting of the Phare Management Committee gave a positive opinion on the ACCESS programme, the successor to the LIEN and Partnership programmes. Activities eligible for ACCESS funding must be related to the adoption of the *acquis* in the fields of environmental protection, socio-economic development or the promotion of sustainable health and social support for marginal groups within the population. Unlike the centrally managed LIEN and Partnership programmes, ACCESS will be implemented locally by the Commission Delegations in the candidate countries.

▪ Horizontal Programme for Justice and Home Affairs

Under the 1996 Phare Horizontal Programme for Justice and Home Affairs, three projects were launched in February 1999 (and will run until December 2000)

- training for police (€ 4.5 million); the contractor is the Association of European Police Colleges (AEPC) and ten Member States are taking part in the implementation of the project
- transfer of the *acquis* in the field of asylum (€ 3 million); this project is led by German Bundesamt für Anerkennung ausländischer Flüchtlinge (BAFl), with the support of the United Nations High Commissioner for Refugees (UNHCR) and seven Member States
- fight against organised crime and corruption (€ 1.5 million), which is being implemented by the Council of Europe.

The 1999 Phare Horizontal Programme for Justice and Home Affairs will cover four sectors: training of judges in European Community law (€ 1 million), rule of law (€ 3 million), judicial cooperation in penal matters (€ 2 million) and migration, visa and border management (€ 3 million). Projects are expected to start in September 2000. As under the 1996 Programme, Member States and international organisations will lead the projects.

▪ Drugs Programme

The Drugs Programme continued to focus on the translation of EU drug priorities into actions. The programme facilitated the implementation of the *acquis* in the field of drugs and the development of national strategies, consistent with the EU approach. In 1999, various projects and activities were completed under the programme, bringing significant results in the three areas of drug policy development, drug demand reduction and drug supply reduction.

In the field of drug information, the programme implemented activities in line with the European Monitoring Centre for Drugs and Drug Addiction and the network of EU National Focal Points. One of the main outputs was the publication of National Reports on the state of the drug problem in 11 partner countries. In this way, the work contributed to the development of comparable drug information systems at European level and helped to further the integration of the candidate countries into the Centre's activities.

A major technical assistance demand reduction project was finalised in 1999. This project established resource centres and strengthened drug demand reduction strategies in all Phare partner countries, increasing their preventive and harm reduction impact and harmonising them with the strategies prevailing in EU countries.

In the field of money laundering, a final assessment concluded that, in most of the candidate countries, the legislation in this area generally meets EU requirements. Substantial progress was also made under the joint Phare-UNDCP drug law enforcement programme in southeastern Europe. Additionally, a number of important new supply reduction projects were designed and launched:

- the drug police personnel exchange programme under which approximately 90 police officers will be exchanged between EU Member States and the candidate countries
- the last phase of the precursors' project, which will continue to focus on the implementation of EU compatible legislation, inter-agency coordination and cooperation with the industry
- as synthetic drugs have been identified as one of the main challenges under the new EU Action Plan to Combat Drugs 2000-04, a project was designed to strengthen measures and capacities to combat the illicit production of and trafficking in synthetic drugs and to prepare the candidate countries for participation in the EU Early Warning System.

Finally, 1999 also witnessed the preparation of a large project (€ 2 million) aimed at increasing the role of civil society in combating drugs. This project will strengthen the institutional capacities of selected drug demand reduction NGOs in the partner countries and will reinforce national strategies on the prevention of drug dependency and associated risks.

▪ **Environmental Programme**

1999 saw the launch of two accession-driven initiatives:

- ◆ the Sustainable Nature Protection Project (€ 1.9 million);
- ◆ *ad hoc* assistance to the candidate countries in preparation for membership of the European Environment Agency (total funding € 3 million).

Meanwhile activities within the framework of the Black Sea Environmental Programme and the Project Preparation Facility were brought to completion at the end of the year.

In addition, a number of sizeable investment projects were launched during the course of 1999

- ◆ Budapest Municipal Waste Water Programme (€ 16 million)
- ◆ Small Municipalities Environment Programme (Estonia, € 6 million)
- ◆ Leipaja/Madona Environment Project (Latvia, € 6.6 million)
- ◆ Klaipeda/Panavezys Environment Project (Lithuania, € 10.2 million)
- ◆ Maribor Water Concession (Slovenia, € 6.5 mil'ion).

▪ **Customs Programme**

In 1999, the customs component of the multi-beneficiary Transit Facilitation and Customs Modernisation Programme focused on preparing the partner countries' customs administrations for accession in two main areas: 'strategic management development' and 'improvement of operational capacity'.

The 'strategic management development' area was addressed with pre-accession meetings and workshops, with a view to completing the processes of comparing the current situation in each country with the Commission's Customs Blueprints and subsequently identifying detailed requirements for assistance (needs-analysis). The partner countries' customs administrations consequently defined their main priorities in the pre-accession period and most of them developed Customs Business Strategies. In addition, the top management of the customs administrations in the candidate countries developed a better understanding of core EU systems, the implications of accession on organisational and personnel issues and relations with the trading community.

The results of the gap- and needs-analyses, along with the approved strategies and annual plans, create a sound basis for the strategic update of the customs chapter within the National Programmes for the Adoption of the Acquis (NPAAAs) and for strategic project proposals within the framework of Phare and other Commission Programmes at national level.

The 'improvement of operational capacity' area was addressed through the continuation of a number of major projects, in different stages of implementation:

- ◆ 'general customs technical assistance and training', involving 12 partner countries, aimed at providing assistance to the customs administrations in key

areas of the customs business, in line with both the Commission's pre-accession strategy and the approved sectoral strategies;

- ◆ 'measures to improve efficiency at border posts', successfully implemented in 11 partner countries, aimed at implementing risk assessment, selectivity and profiling tools and techniques in the operational customs environment, through the creation/improvement of national training teams/programmes;
- ◆ 'customs information and intelligence', involving 12 customs administrations, aimed at creating/improving national 'intelligence' systems, teams and programmes and implementing 'intelligence' tools and techniques in day-to-day customs operations, through the use of information already available within the customs administrations concerned;
- ◆ 'transit north-south', implemented in six partner countries, aimed at preparing the legal and institutional framework for the final implementation of the Common Transit Convention and the EU new computerised transit system.

Programme management

Deconcentration and decentralisation

In the context of Phare, decentralisation means the transfer of management responsibilities from the European Commission to the candidate countries. Deconcentration describes the transfer of responsibilities within the Commission from its Headquarters in Brussels to its Delegations in the candidate countries.

▪ Deconcentration

The new Phare guidelines (1998) foresaw an increased responsibility for Commission Delegations in candidate countries in the supervision of the implementation of Phare. This policy was reconfirmed in the 1999 Phare guidelines, as it is an important step towards the further decentralisation of the Programme to the countries themselves.

A certain level of deconcentration already existed with respect to the approval of contracts under the Phare Decentralised Implementation System, whereby the Head of Delegation had responsibility for endorsing contracts up to € 500,000. The Head of Delegation now has authority to approve tender documents and evaluations and to endorse contracts up to € 5 million.

The objective was to ensure that deconcentration was implemented in all candidate country Delegations as quickly as possible. The precise timing has depended on a strengthening of each Delegation's administrative capacity, through the introduction of more rigorous internal procedures and the recruitment of a Financial Officer in charge of checking the correctness of Phare procurement. Following the recruitment of local agents and Financial Officers and appropriate training, deconcentration was introduced in all the ten Delegations concerned by June 1999.

▪ Decentralisation

As part of the preparation of the candidate countries for accession, the policy of decentralisation of the implementation of the Phare Programme to the candidate countries was continued. This meant that, to the extent permitted by the European Communities' Financial Regulation, the implementation of national programmes will be the responsibility of the candidate countries, under the supervision of the European Commission – which remains ultimately responsible for the use of the funds.

As part of the decentralisation process, centralised contracting by the Commission for national programmes was terminated. The candidate countries now conclude all contracts in the national programmes.

The criteria for further decentralisation of the Phare Programme (together with ISPA and SAPARD) were laid out in the Coordinating Regulation of the Pre-accession Instruments (1266/99). Accordingly, further decentralisation will only be authorised by the Commission on a case-by-case basis in those sectors where the criteria defined in the Annex of the Coordinating Regulation are respected by the candidate country

and the implementing agency responsible. This will ensure sound and efficient management and transparency of the use of the funds in line with the objectives of the agreed programmes. The partner country will commit itself to respecting the rules governing Phare as well as the Community's Financial Regulation. Candidate countries will be financially accountable and, if the rules are not respected, funds will be recovered by the Commission.

Implementation structures in partner countries

The new implementation structures launched by the new Phare guidelines became operational in all candidate countries in 1999. In each candidate country there is now a National Fund, headed by a National Authorising Officer, in charge of the financial management of the programme. The actual implementation is carried out by Implementing Agencies. An implementing agency - a Central Finance and Contracting Unit (CFCU) - is specifically in charge of tendering and contracting institution building projects, whilst the beneficiary ministries are responsible for project selection and monitoring.

Monitoring and evaluation

The regular monitoring and assessment (M&A) of Phare programmes was introduced in 1996. M&A reports are essentially a management tool which provide Phare programme managers with facts on the implementation of on-going programmes and an assessment of the progress and likelihood of a programme's success in achieving the objectives set. Recommendations are put forward for improving management and delivery, as well as the design of similar future programmes. The reports are also used when an *ex-post* evaluation is carried out on a particular sector.

By the end of 1999, some 300 reports had been produced, covering all sectors in all Phare Programme recipient countries.

In line with deconcentration, monitoring of programmes will now be done locally, with an independent and external assessment as a complementary activity.

Joint Monitoring Committees (JMCs) and Sectoral Monitoring Committees (SMSC) have been established in the ten candidate countries. The JMC is responsible for reviewing the progress of all Phare programmes implemented in the respective country, once a year (as well as ISPA and SAPARD programmes). The SMSC must submit monitoring reports at least twice a year on all programmes in the country in the relevant sector. The JMC may make recommendations to the Commission on the development of on-going programmes.

Responsibility for monitoring will lie with programme implementors (Implementing Agents, CFCUs, etc.), who will be responsible for reporting regularly on implementation in accordance with a template and criteria to ensure uniformity of approach.

Financial overview and performance

In 1999, the Phare Programme committed a total of € 1,481.62 million to its partner countries. The following chart shows the break down year by year of the Phare funds committed in the period 1990-1999 (€ million):

1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
475.3	769.7	979.6	966.1	946.1	1,114.0	1,207.8	1,135.1	1,153.9	1,481.7

The situation with regard to implementation may be summarised as follows:

Total commitments 1990-1999	€ 10,229.19 million
Total value of contracts signed 1990-1999	€ 7,915.16 million (thus 77.4 per cent of all commitments have been contracted)
Total payments under signed contracts 1990-1999	€ 6,355.13 million (thus 62.1 per cent of all committed funds have been paid and 80.3 per cent of all contracted funds have been paid).

Phare in the individual partner countries

Candidate countries

Bulgaria

The year in review

Despite the unfavourable external environment, macroeconomic developments in Bulgaria have remained relatively positive since mid-1998. Economic activity and real incomes have recovered from the depressed levels of early 1997, inflation has been reduced to low levels and the currency has remained stable.

However, the Kosovo crisis has affected the still-fragile economy. GDP growth started to slow down in the second half of 1998; weak industrial sales and negative developments in external accounts in early 1999 pointed to a continued deceleration of GDP growth. The Bulgarian authorities revised their GDP growth forecast for 1999 down from 3.7 per cent to 1.5 per cent. Despite the termination of the military campaign, the aftermath of the Kosovo crisis was expected to lead to a further deterioration of Bulgaria's external accounts and to affect growth prospects for 1999.

There was further progress in the reduction of inflation thanks to the stabilising effect of the currency board and the fall in international commodity and energy prices. Year-on-year inflation declined to 1.3 per cent in July 1999. As in both 1997 and 1998, fiscal performance was better than expected. The 1999 budget provided for an overall deficit of 2.8 per cent of GDP. However, in view of the widening current account deficit, the authorities adopted a general government deficit target of 2 per cent of GDP in May. A higher-than-expected surplus was recorded in the first half of 1999.

Although progress on privatisation slowed somewhat in 1998, the authorities set themselves the target of privatising all commercial enterprises, as well as a significant number of utilities, by the end of 1999. Significant progress was achieved, with the successful privatisation of the Bulgarian telecoms company in July, for over € 450 million. With United Bulgarian Bank and Postbank already privatised, three out of the four remaining state banks were expected to be privatised in 1999.

Measures to increase the efficiency of the tax administration continued. The 1999 budget pursued the reform of the tax system initiated in 1998 by reducing the VAT rate, eliminating most remaining exemptions and lowering the corporate tax rate. As part of the healthcare reform, a 6 per cent payroll tax was introduced on 1 July 1999. Implementation of the reform programme continued, with adoption of legislation on healthcare reform and laws designed to streamline facilities and employment in the healthcare sector. Preparation of the reform of the pension system also continued.

In the banking sector, measures were taken to strengthen banking supervision and improve the efficiency of the sector. A self-financing deposit insurance system was introduced in January 1999; in addition, prudential standards were strengthened and the central bank empowered to ensure compliance with these rules. As a result the banking system is relatively sound and highly capitalised. However, the sector still suffers from high operating costs and low profitability.

With regard to enterprise reform, progress was made in limiting the losses of state-owned enterprises and promoting their restructuring by isolating the major loss-makers from the banking system. The isolation programme was completed for

commercial enterprises by June 1999. However, progress in restructuring utilities was less satisfactory. The government decided to freeze the wage-bills of loss-making state-owned companies in the first half of 1999.

The political situation remained stable in 1999. The Parliament continued to operate smoothly; its powers are respected and the opposition plays a full part in its activities. Policy making in the central institutions has improved but remains rather weak; coordination between officials of different ministries needs to be strengthened. There has been some progress with the entry into force of the Law on State Administration and the Civil Service Law. Judicial reform needs to continue and would benefit from the preparation of an overall strategy, including measures to increase the effectiveness and transparency of the judicial system.

The reform-oriented majority under the leadership of the United Democratic Forces helped to secure continued support for market economy reforms and the further integration of Bulgaria with the EU and the Euro-Atlantic bodies. Commitment to EU membership remains high on the government agenda. Bulgaria also continued to prepare for NATO membership. Its commitment to membership was underlined again during the Kosovo conflict when Bulgaria was firmly supportive of EU action and aligned itself to all EU and NATO positions.

In May 1999, Bulgaria presented a revised National Programme for the Adoption of the Acquis (NPAA), in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. A Joint Assessment of Bulgaria's Medium-Term Economic Policy Priorities was signed in June 1999. The meetings of the Association Council and Association Committee were held in November and July 1999 respectively. 1999 also saw the publication of the second Regular Report (see box below) on Bulgaria's progress towards accession.

Conclusion of the European Commission's Regular Report, October 1999

Bulgaria fulfils the Copenhagen political criteria. However, further efforts need to be undertaken to strengthen the rule of law and protect human and minority rights, particularly in relation to the Roma population, where recent government decisions need to be followed by concrete measures together with appropriate financial resources. Particular attention needs to be paid to fighting corruption and improving the functioning of the judicial system.

Bulgaria has continued to make progress in establishing a functioning market economy but further steps are needed and it is not yet in a position to cope with competitive pressures and market forces within the Union in the medium-term.

Bulgaria has made determined efforts to put in place the key elements of internal market legislation. A new law on public procurement sets out the basic principles of the *acquis* and there has been progress in the area of standardisation. There has also been progress in the fight against piracy, the alignment of audio-visual legislation, liberalisation of the telecommunications market and the introduction of new VAT and

excise laws. In all these areas there is a need to pay particular attention to the capacity of the administration to implement and enforce legislation.

There has been no significant improvement in the area of state aids. Despite some progress in alignment with the agricultural *acquis*, there are problems of implementation. There has been some legislative progress in the environmental field but the lack of an overall strategy and sectoral strategies continues to pose problems. Bulgaria has made significant progress in the area of justice and home affairs, particularly in the fields of immigration and justice.

Although Bulgaria has taken some steps in developing energy policy, it has made no progress in committing itself to a realistic timetable for the closure of Units 1-4 at Kosloduy nuclear power plant, despite the fact that this was a short-term priority of the Accession Partnership.

The adoption of a Civil Service law indicates that the government intends to pursue its efforts to strengthen administrative capacity. Progress has been made in establishing the legal framework for setting up the institutions responsible for the application of EU legislation and many of the structures have been set up. However, the shortage of human and financial resources has hampered the capacity of these institutions to effectively implement the *acquis*.

Bulgaria has made progress in meeting all of the short-term priorities of the Accession Partnership except as regards the nuclear sector.

Phare in 1999

A total of € 123.7 million was allocated to Bulgaria under the 1999 Phare budget to support Bulgaria's accession to the EU. The relevant Financing Memoranda between the European Commission and Bulgaria were signed in December 1999.

Phare support for Bulgaria's accession preparations was channelled through four main programmes: the National Programme (€ 52.1 million), the Cross-Border Cooperation Programme with Greece and Romania (€ 30 million), the Large-Scale Infrastructure Facility (€ 25.7 million) and the Catch-Up Facility (€ 14 million). Bulgaria also received funding under the Consensus III programme (€ 1.9 million), as well as for participation in Phare multi-beneficiary and horizontal programmes, including those on customs, democracy, standardisation, SMEs, nuclear safety, environment, statistics, public administration reform and TAIEX.

The **1999 Phare National Programme** focused on the following priorities identified in Bulgaria's Accession Partnership

- **integration of the Roma** (€ 0.5 million): improving education, living standards and access to jobs for the Roma population
- **economic reform** (€ 4.8 million): providing management training and capacity building for the national SME agency and regional network

- **institutional capacity** (€ 4.5 million): establishing the national institute for public administration and EU integration; strengthening the Ministry of Finance (partly delivered by twinning)
- **internal market** (€ 2 million): reinforcing capacity to manage competition policy and control state aids (partly delivered by twinnings)
- **justice and home affairs** (€ 9.5 million): strengthening border management, the police and the judiciary (partly delivered by twinnings)
- **environment** (€ 4.9 million): aligning legislation, providing *acquis*-related investment and strengthening the institutional framework (partly delivered by twinning)
- **agriculture** (€ 10.3 million): upgrading veterinary and phytosanitary sectors, improving seed control and aligning agricultural statistics and viticulture legislation (partly delivered by twinning)
- **employment and social affairs** (€ 4.5 million): Beautiful Bulgaria II temporary employment and training scheme.

The 1999 National Programme also included support to help Bulgaria finance its contributions to a number of Community programmes (€ 8.7 million) and a project preparation facility (€ 2.5 million). Tempus has continued the activities of the successful Joint European Projects and of the Individual Mobility Grants in 1999 with an allocation of 1.637.495 € for 14 projects.

The **1999 Cross-Border Cooperation Programme** had the following main components

- Greece-Bulgaria (€ 25 million): railway electrification, road rehabilitation, optic cable installation, uranium mine closure and project preparation facility
- Romania-Bulgaria (€ 5 million): modernisation of border equipment at gas pipeline crossing, Rousse railway bridge, Danube winter camp, air quality monitoring and cooperation development plan.

The **1999 Large-Scale Infrastructure Facility** was devoted largely to the construction of the Sofia waste water treatment plant (€ 23 million), with an additional element to support project preparation for the new ISPA instrument (€ 2.7 million).

The **1999 Catch-Up Facility** had two elements: a steel and mining area employment programme (€ 12 million) and further support for Bulgaria's programme to attract foreign direct investment (€ 2 million).

Including the 1999 allocation, Phare grant funding to Bulgaria since 1989 now stands at almost € 866 million.

A number of ongoing Phare programmes made good progress during 1999.

Phare has been providing support to the **vocational education training** system since 1995. In 1999, projects were successfully completed in a range of areas, including the development of new curricula and teachers' qualifications. New training equipment was provided and a decentralised financial management system for schools was put in place.

In the **social sector**, Phare continued to support active labour market measures to reduce unemployment. In 1999, the Beautiful Bulgaria programme created 18,000 man-months of employment and upgraded the urban environment of several Bulgarian cities. The programme will continue to help create employment opportunities in 2000.

The first **twinning** agreements for projects under the 1998 programme were finalised in 1999. Seven pre-accession advisers were in place by the end of 1999, with three more expected early in 2000.

Implementation of the Phare Programme in Bulgaria was generally satisfactory in 1999. At the end of 1999, the programmes for 1997 and earlier years were almost fully contracted, while the 1998 programme was about 40 per cent contracted.

Phare implementation became fully 'deconcentrated' in Bulgaria in mid-1999, following the appointment of a Financing Officer at the EU Delegation in June. Deconcentration has allowed the Delegation to play a more active, rigorous and systematic role in monitoring implementation of Phare programmes.

Following its establishment in 1998, the National Fund signed financing agreements with the CFCU and eight Implementing Agencies. Phare is supporting some transitional assistance to strengthen the capacity of the National Fund and CFCU. With the gradual closure of pre-1998 programmes, PMUs are now being phased out. The Delegation has established quarterly local Implementation Review Meetings with all Bulgarian counterparts that have on-going Phare programmes. The first of a series of workshops on Phare financial management and contracting was held by the Delegation in December 1999 with representatives of the National Fund, CFCU, PMUs and Implementing Agencies.

Results

Launched in 1997 and continued under the 1998 National Programme, the Phare **Structural Adjustment Reform Assistance (SARA) programme** has been a remarkable success. SARA supports the Government's economic reform and private sector development programme, drawn up in close collaboration with the IMF and World Bank. There has been major progress in divestment and liquidation: all the main enterprises, apart from utilities, are now in private hands and significant foreign investment has been attracted in the process. SARA has contributed directly to the sale of 20 major enterprises and one major bank. SARA has been essential in helping the Government meet its commitments under successive loan agreements with the international financial institutions.

SARA has supported the development of a medium-term strategy for restructuring the Ministry of Finance and contributed to fiscal consolidation by helping the Ministry monitor and control the losses of the remaining state-owned enterprises.

As the privatisation process nears completion, Phare support for **economic reform** is changing its focus towards helping create a more conducive environment for private sector development and inward investment. Under the 1998 programme, Phare is

providing consultancy services to newly privatised companies and helping to strengthen the capacity of the National SME and Foreign Investment Agencies.

Phare has been actively supporting **regional development** in Bulgaria since 1997. This has involved policy advice and institution building at central and regional levels, to prepare the country to handle the new pre-accession financial instruments and, after accession, the structural funds.

In 1999, Eurostat completed a regional classification of the national territory and the Government decided that six NUTS-II-type planning regions would be used as the basis for regional policy. With Phare support, the Bulgarian authorities prepared a preliminary **National Development Plan**, which could eventually evolve into a Community Support Framework for structural funds purposes on accession. This was the culmination of many months of inter-ministerial dialogue and analysis at the central and regional levels, coordinated by the Ministry of Regional Development and Public Works. The Plan incorporates sector strategies and regional priorities within an overall framework of national development objectives. The regional development section of the plan selects two of the six regions for Phare investment to support economic and social cohesion from 2000 onwards. The authorities within these regions are being made familiar with EU regional and structural funds practices to help them manage projects.

Phare has been actively supporting the development of **civil society** in Bulgaria, under both the national and multi-country programmes. A Civil Society Development Foundation was set up to reinforce the non-profit sector and civil society more generally. Part of the Foundation's activities consist of financing projects proposed by local NGOs. The number of registered NGOs has grown to over 8,000, of which about 5,000 are considered active. An increased NGO role in lobbying, advocacy and campaigning can also be observed.

Phare has been providing support to the **agricultural sector** since 1990. Support under the 1999 Phare Programme focused on plant health and veterinary control, integration policy and the preparation of the country for the SAPARD pre-accession funds. Four institution-building projects involving twinning were launched (in the veterinary, plant health, approximation of legislation and SAPARD areas) while technical assistance projects were launched for CAP and common market organisations; large equipment procurement tenders for the country's veterinary and plant health laboratories were also prepared.

Case study: Vocational education & training (VET) development

This project was intended to develop new curricula for selected professionals in vocational schools, building upon post-secondary module curricula developed in an earlier Phare Programme. It also provided teacher training to apply the new technologies, as well as new technological and learning equipment. The project started in November 1996 and was successfully completed in December 1999. It had a budget of € 3.7 million, including € 1.4 million for equipment for pilot schools.

The project achieved the following results

- a long-term VET policy paper for Bulgaria was prepared, which contributed to the preparation of the new VET Law, ratified by Parliament in July 1999
- a VET National Agency was formally established, with responsibility for awarding school accreditation, issuing licenses for training and career guidance centres and developing national standards for vocational qualifications
- new curricula were developed in 18 vocational categories and new courses are now in use in 41 schools throughout the country
- training equipment was provided in 18 vocational categories for 35 pilot project schools
- curriculum evaluation instruments were developed for schools and local consultants were trained in evaluation procedures
- internal and external assessment verification systems were established for each pilot school.

Czech Republic

The year in review

The macroeconomic situation in the Czech Republic remained difficult in 1999. Real GDP continued to fall, unemployment rose significantly and real incomes contracted. The downturn in the economy has proved deeper and lengthier than expected and macroeconomic prospects are only slowly improving. Nevertheless, there have also been some positive signals: the country's export position has improved and inflation has reached a level comparable to that in the EU. The current macroeconomic problems have highlighted the need to proceed quickly with remaining structural reforms.

The economic recession deepened in the first part of 1999, with the economy contracting by 4.1 per cent in the first quarter when compared with a year earlier. However, in the second quarter of 1999 a recovery seemed to be emerging, with real GDP growth of 0.3 per cent year-on-year. Similarly, real export growth weakened in early 1999 but recovered somewhat in the second quarter. On the output side, almost all sectors contracted, except the trade sector, financial services and agriculture. The unemployment rate rose steadily as the recession deepened. In December 1999, the unemployment rate had reached 9.4 per cent (compared to 6.8 per cent in October 1998).

On the positive side, in the first half of 1999, both the trade deficit and the current account deficit were down significantly on their 1998 levels. The current account deficit was fully covered by a surplus on the financial account. In particular, foreign direct investment inflows accelerated: € 1 billion in the first half of 1999. Inflation continued to fall: 12-month consumer price inflation was down to 1.4 per cent in August 1999 compared with 8.2 per cent in October 1998.

Structural reform was pursued with the continued cleaning up of the banking sector. Banking privatisation accelerated in 1999: on 10 March the government announced an ambitious timetable for the remaining privatisations. This culminated in agreement on the sale of CSOB to a Belgian bank for over € 1 billion at the beginning of June. The sale of two other banks should be completed by mid-2000. The government has been considering the privatisation of certain utilities, but does not wish to begin before adequate framework legislation is in place.

The main government initiative in the area of structural reform was the adoption in April of a programme for the revitalisation of industry, with the aim of providing renewed access to financing for major industrial companies experiencing financial difficulties, mainly due to a lack of effective restructuring since privatisation. Finally, the government attempted to extend its investment incentives package, including a five-year tax holiday, duty free technology imports, the possibility of creating duty free zones and subsidies for training. Several sets of concessions were approved by the Cabinet and line ministries over the summer of 1999.

Despite considerable efforts by the government, progress remained limited in terms of adopted legislation and improvements in administrative structures. The delay in implementation of government policy is due to the length of procedures for preparing

draft legislation by the ministries and of the parliamentary process itself, the minority status of the government and the fact that certain priority areas had not received sufficient attention from previous governments. The government's proposal to amend the constitution to enable it to approve accession-related legislation by decree was rejected by Parliament in May.

The performance of the state administration remains affected by the absence of a unified system of public administration. The administration continues to suffer from inadequate management, lack of training, low pay and lack of coordination between ministries. Regarding the judiciary, judges are not sufficiently specialised and have to perform time-consuming administrative tasks. The courts suffer from a lack of modern equipment and information technology. There is still a large number of vacancies for judges and state attorneys. Finally, the performance of the judiciary in the fight against organised and economic crime remains weak.

In March 1999, the Czech Republic acceded to NATO and decided to join sanctions against Yugoslavia. The Government adopted the draft medium-term social and economic policy priorities for the period 1999 to 2002 in May, with the Joint Assessment exercise starting shortly after. Less positive developments include an incident in October in the town of Usti nad Labem when a fence separating the Roma from non-Roma residents was replaced by a concrete wall; following condemnation by Parliament, the government and the EU, the wall was taken down a few weeks later. 1999 was marked by continuing discussions between the political parties on reinforcing or replacing the minority government. However, there seemed to be no alternative to the 'Opposition Agreement', whereby the government of Social Democrats is supported by the main opposition party.

EU accession remains a priority of the government, which expressed its agreement with the conclusions of the European Commission's 1998 Regular Report and decided to speed up preparations for accession in priority areas. The Association Committee met in May 1999 and examined the implementation of Accession Partnership priorities. In June 1999, the Czech Republic presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. 1999 also saw the publication of the second Regular Report (see box below) on the Czech Republic's progress towards accession.

**Conclusion of the European Commission's Regular Report,
October 1999**

The Czech Republic fulfils the Copenhagen political criteria. Further efforts should be made to reform the judiciary and improve the situation of the Roma through the implementation of an adequately funded policy and efforts to combat discriminatory attitudes in society. Attention should also be paid to developing an effective policy to combat economic crime and corruption.

The Czech Republic can be regarded as a functioning market economy. It should be able to cope with the competitive pressures and market forces within the Union in the

medium-term, provided that the government accelerates implementation of legal and structural reforms.

The pace of legislative alignment in the Czech Republic has not picked up significantly and progress is uneven across sectors. Alignment is well advanced in the areas of standards and certification and customs and border enforcement. Further progress has been made in the liberalisation of capital markets.

In other key internal market areas such as intellectual property, public procurement, data protection, insurance, anti-trust, state aids and VAT/excise, legislation is already partially aligned but there has been little progress toward completing alignment. There has been little progress in the areas of state aids, the alignment of audio-visual legislation, the adoption of environment framework legislation and alignment in the transport (with the exception of air transport) and agricultural sectors. Apart from adopting laws on drugs, efforts in the area of justice and home affairs have stalled.

The Czech Republic has taken limited steps toward general public administration reform. The government has approved a programme for the overall reform of the judiciary. Capacities in certain areas of the internal market *acquis* are well developed and progress has been made in strengthening banking and financial service supervision capacities. Little progress has been made in setting up the structures necessary for the implementation of the Common Agricultural Policy.

The Czech Republic's record in terms of meeting the short-term Accession Partnership priorities is not satisfactory, despite efforts by the government to prepare and put forward legislation. While the Czech Republic met the short-term Accession Partnership priorities in areas such as economic reform, standards and certification, regional development and veterinary standards, priorities in the areas of industrial restructuring, administrative capacity, the internal market, justice and home affairs and the environment have not been adequately dealt with.

Phare in 1999

In July 1999, the European Commission and the Czech authorities signed the financing memorandum for the 1999 Phare National Programme for the Czech Republic, which amounted to € 16 million. In line with the 1998-1999 Phare Guidelines, the 1999 National Programme focused on the short-term priorities of the Accession Partnership, as well as a limited number of activities in support of medium-term priorities.

The **1999 Phare National Programme** concentrated on the following main priorities

- strengthening the **democratic system**, the rule of law, human rights and the protection of minorities, in particular in relation to the Roma (€ 0.5 million)
- providing support in the area of **economic and social cohesion**, including SME promotion and employment measures (€ 5.35 million)
- strengthening **institutional and administrative capacity** to manage the *acquis*, in particular in the area of public finance, phytosanitary standards, occupational health and safety and the environment (€ 5.8 million)

- providing support in the area of **justice and home affairs**, focusing on the fight against organised and economic crime and strengthening border management and the judiciary (€ 4 million)
- providing Phare **management support** (€ 0.15 million).

Also included in the 1999 national allocation for the Czech Republic, but the subject of separate financing memoranda, was Phare support for the Czech Republic's further participation in various Community Programmes (€ 4 million Tempus has continued the activities of the successful Joint European Projects and of the Individual Mobility Grants in 1999 with an allocation of 570.547 € for 6 projects.

An additional € 29.4 million was allocated to the **Cross-Border Cooperation Programme** with Germany, € 10.6 million for cooperation with Austria, € 3 million for cooperation with Poland and € 2 million for cooperation with Slovakia. The Czech Republic also continued to participate in and benefit from Phare-funded horizontal programmes such as TAIEX, Consensus III, the Small and Medium-Sized Enterprises Facility and the Large-Scale Infrastructure Facility.

1999 saw the start of implementation of the first Phare **twinning** projects in the Czech Republic. Under this new scheme, originally launched in 1998, a total of eight twinning projects got under way providing long-term assistance for restructuring of the Ministry of Agriculture and the Market Intervention Agency, strengthening environmental law enforcement bodies, preparing for Structural Funds implementation, strengthening border control, developing law enforcement institutions and promoting the independence of the judiciary. Under the 1999 Phare Programme, ten twinning projects are foreseen in areas such as occupational health and safety, the fight against economic crime, control and management of EU financial flows, indirect taxation and preparation for Schengen implementation.

As regards **Phare programme management and implementation** in 1999, € 86.2 million of Phare funds was committed to the Czech Republic for projects to be implemented over the 1999-2001 period; 1999 saw Phare-financed contracts signed for the largest ever amount of Phare funds in the Czech Republic in any one year, with contracts worth a total of € 118.3 million. To date, a total of € 625.4 million has been committed to the Czech Republic under the Phare Programme. € 498 million of this total has been contracted (79 per cent of the amount committed, as opposed to 70 per cent at the end of 1998 and 53 per cent at the end of 1995). A total of € 127.3 million remains to be contracted in 1999 and 2000 (20 per cent). Disbursement in 1999 amounted to € 77 million.

Results

Within the framework of preparing for the **Structural Funds and regional development**, Phare supported the production of regional development plans and the National Development Plan (NDP). The process of preparation of these plans was very positive, with a high level of participation from the regions and the public, private and NGO sectors. The NDP will be developed further and provides the basis on which Structural Funds should be allocated to the Czech Republic once it has acceded to the EU. Phare also established a € 2.5 million regional development fund, which provides co-financing to municipalities for the creation of sites to support industry and SMEs.

Phare continued to play an important role in co-financing government support to **private sector development**. During 1999, Regional Business Advisory Centres and Business Innovation Centres continued to provide advice, training and cheap accommodation for businesses. Phare support for CzechTrade has helped to establish it as an active and well-respected trade promotion organisation. Following the success of the Phare-financed venture capital fund in Ostrava, the returns have been re-invested in a new fund in North-West Bohemia. Finally, SMEs continued to benefit from revolving small-loans schemes financed by Phare; over 1,000 companies have received loans to date.

With regard to **infrastructure and environment**, the largest Phare project in the Czech Republic (€ 34 million from Phare) - the improvement of the Brno-Vranovice railway line (part of the Prague-Vienna line) - was continued and was nearing completion at the end of 1999. Three road projects were commenced and one completed totalling € 7.4 million. The first stage of the Phare Energy-Saving Fund (€ 10 million) was completed; all the funds were disbursed through 25 loans and repayments, which have already begun, will be used to make loans of a similar nature during the next ten years. Many more environmental projects have been financed from the Cross-Border Cooperation Programme (see box below).

The first Phare-financed twinning project started in the Czech Republic in May 1999 in the **agricultural sector**. Together with the Phare-financed Policy Advisory Unit, the Pre-Accession Advisor from the German Federal Ministry of Agriculture is working to ensure that the Czech Republic is prepared for the implementation of the Common Agricultural Policy and that the requisite mechanisms are in place. The first major Phare-financed twinning projects in the field of **justice and home affairs** also began, advising on the training of border police and the improvement of human resources management in the police force as a whole.

In the area of **employment and social affairs**, Phare supported projects to improve the Czech Republic's occupational safety inspectorate and to digitalise the social welfare administrative system. As the employment situation in the Czech Republic worsened, the Phare-financed loan scheme PALMIF made grants totalling over € 1.5 million available to help protect jobs.

Case study: Cross-Border Cooperation (CBC)

Since 1994, the Phare CBC Programme has helped to promote cooperation between border regions of EU Member States and neighbouring candidate countries. It also aims to address the disparity in living conditions between the peripheral regions and the centre of the Czech Republic. The programme primarily co-finances infrastructure measures in the regions bordering on Germany and Austria and, in 1999, Poland and Slovakia as well. Projects are proposed and the necessary co-financing arranged by Czech municipalities.

The CBC Programme is a concrete example of a regional investment programme which can make a real difference to the border regions - particularly to North-West

Bohemia, one of the most deprived regions in the country. Since the CBC Programme has involved local bodies from the outset, expertise in the use of EU funds is spread throughout the country and should prove most useful when the Czech Republic starts to receive Structural Funds. The CBC Programme has significantly improved the infrastructure of the border regions and compliance with EU standards. Typical projects are waste water treatment plants and the construction of gas pipelines, which help reduce water and air pollution.

Regional Development Agencies oversee the CBC-financed Small Project Funds (SPFs), which make funds available to organisations or individuals for small people-to-people cross-border projects, such as cultural exchanges. Over 1,200 projects have been financed to date, receiving on average € 3,500 each in Phare funds. The projects have helped to develop closer contacts between people, complementing the larger infrastructure measures which improve the physical environment.

To date € 183 million has been committed to the CBC Programme; € 113.3 million for major construction projects and € 17.5 million for SPFs. The remainder of the funds has supported the development of tourism, the business environment and regional studies. Six road and three railway improvements, twenty waste-water treatment plants, three gas pipelines and three renovations of historic buildings have so far been completed.

Estonia

The year in review

The Estonian economy has experienced a sharp slowdown since the second half of 1998. While this decline has led to an increase in unemployment and has swung the budget into deficit, macroeconomic stability has been preserved. However, the slowdown has revealed some underlying structural weaknesses in the economy. This has reinforced the need to accelerate reforms, many of which had been delayed in the run up to the general elections of March 1999.

The Estonian economy has suffered a very rapid fall in activity since mid-1998. Real GDP has fallen continuously since the last quarter of that year. Domestic demand has also weakened considerably due to slower credit growth, higher investment rates and lower business confidence. The labour market has been affected by the decline in growth, with registered unemployment increasing by a third between October 1998 and August 1999, to 5 per cent of the workforce.

The Russian crisis continued to have negative effects: in July 1999, exports to Russia represented only half of the level reached in July 1998. The year-on-year growth of exports and imports became negative in 1999, due to the fall in exports to the east and a reduction in domestic demand. The sharp drop in imports led to a reduction in external imbalances. In 1999, the decline of both the current account and trade deficits continued; in the first half of 1999, the current account deficit amounted to less than 7 per cent of GDP. Lower economic activity had a negative impact on fiscal revenues. As a result, the general government accounts swung from a surplus in June 1998 to a deficit of 3.1 per cent in mid-1999.

Inflation has slowed down considerably. In August 1999 consumer prices grew by just 2.6 per cent (compared to 6.6 per cent in September 1998), while producer, export and import prices declined. Falling commodity prices and weak domestic demand were the main factors behind this trend. As in 1998, Estonia continued to attract high foreign direct investment inflows in 1999.

Estonia has made further progress on structural issues, particularly as regards financial sector and fiscal reforms. Privatisation has continued, albeit at a slower pace due to the achievements of previous years, and only a small number of companies remains to be sold. In February 1999, the government sold a 24 per cent stake in the national telecommunications company through an international stock offering. It also sold two small electric distribution networks and several divisions of the railways company. However, the privatisation of the oil shale mining, power generation and railways freight companies has been repeatedly delayed.

Reform of the social security system began in early 1998, with steps to introduce a three-pillar system, but progress stalled thereafter. In July 1999, some details were announced on the introduction of the second pillar (fully funded and mandatory) and, in the spring of 1999, the first pension fund under the first pillar (fully funded and voluntary) was granted its licence and started to collect funds.

Reforms in the financial sector continued. There was a drastic cut in the number of banks and foreign investors took controlling stakes in the two largest Estonian banking groups. In 1999, two small banks were declared bankrupt. In addition, the central bank started negotiations to sell the majority stake that it had acquired in the third largest bank in October 1998, in an effort to prevent a systemic crisis during the turbulence on international financial markets.

Progress was made in the area of land reform. At the end of May 1999, about half of the total land of the country was put in the cadastre, while the share of registered private land grew from around 15 per cent at the end of 1997 to 25 per cent in May 1999.

Estonia's parliamentary elections took place on 7 March 1999; the voter turnout was 56 per cent. Of the 12 parties that had registered for the polls, only 7 received the 5 per cent of votes necessary to gain a seat in parliament. These results reflect a trend towards the streamlining of the political picture in Estonia, until now fragmented into many small parties. The Centre Party won the most votes, 23.4 per cent of the total; however, the party did not have enough support to form a government and so a coalition government of the Moderates, Reform and Pro-Patria parties took office. The new government has a liberal, business-oriented programme and is strongly committed to EU accession.

The Estonian public administration continues to suffer from insufficient skills and a high turnover of staff. A continued commitment to public administration reform is needed to create a body of qualified civil servants that can ensure the implementation and enforcement of the EU *acquis*. Although a series of reforms to improve the judicial system have been undertaken, Estonia needs to carry out further adjustments to its legislation in order to complete the transition from the former system. Progress in this area is very slow.

In May 1999, Estonia presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. The second meetings of the Association Council and Association Committee were held in April and June 1999 respectively. The June 1999 meeting was the first occasion to discuss the implementation of the Accession Partnership priorities. Estonia has not yet agreed to a Joint Assessment of Medium-Term Economic Policy Priorities with the European Commission. 1999 also saw the publication of the second Regular Report (see box below) on Estonia's progress towards accession.

**Conclusion of the European Commission's Regular Report,
October 1999**

Estonia fulfils the Copenhagen political criteria. However, the adoption of the Language Law, which restricts the involvement of non-Estonian speakers to political and economic life constitutes a step backwards and should be amended. In the meantime, the Commission will closely monitor the implementation of the law to see what impact it will have in practice. Attention needs to be paid to the fight against corruption.

Estonia is a functioning market economy where market forces play their full role. It should be able to cope with competitive pressures and market forces within the Union in the medium-term, provided it completes the remaining key structural reforms.

Estonia has continued its alignment in the single market area, in particular as regards intellectual property, data protection, free movement of goods and state aid monitoring. The lack of human resources has delayed reform in the area of standards and certification. Progress has been noted in the fields of energy and transport, but restructuring of the oil-shale sector should be a priority, as should fiscal harmonisation in road transport.

Although some progress has been made in agriculture, fisheries and regional development, efforts are needed to develop institutional structures and capacity to manage funds. Considerable efforts are needed on the customs code, tariffs and capacity building. Estonia has followed most of the 1998 Report's recommendations on justice and home affairs, where efforts need to be sustained, particularly regarding the police.

Overall, Estonia has continued to make progress in further aligning its legislation with the *acquis*. Progress has been limited in improving administrative and judicial capacity, where the short-term Accession Partnership priorities have only been partly met. It remains difficult to recruit and retain qualified staff and priority should be given to remedying this situation. Considerable efforts should be made in this respect in particular as regards the free movement of goods, state aids, agriculture, customs, regional policy, environment, financial control and social issues.

Phare in 1999

On 23 August 1999, the Estonian government and the European Commission signed the Financing Memorandum for the Phare National Programme for Estonia. A total of € 23.3 million was allocated to Estonia under the 1999 Phare budget to support Estonia's accession to the EU, in line with the priorities highlighted in the Accession Partnership.

Phare support for Estonia's accession preparations was channelled through three main programmes: the Phare National Programme (with a budget of € 7.2 million), the Cross-border Cooperation Programme (€ 3 million) and the Large-Scale Infrastructure Facility (€ 11 million). Estonia also participated in Phare multi-beneficiary and horizontal programmes in 1999, including TAIEX (approximation of EU legislation), Consensus (social), Justice and Home Affairs and the SME Facility. Tempus has continued the activities of the successful Joint European Projects and of the Individual Mobility Grants in 1999 with an allocation of 311.743 € for 4 projects.

In line with accession priorities, the **1999 Phare National Programme** focused on

- reinforcing the institutional and administrative capacity of **regulatory and surveillance bodies** (€ 2 million)

- reinforcing the institutional and administrative capacity in the **financial sector** (€ 1.5 million)
- developing **police criminalistics** and forensic sciences (€ 2.5 million)
- developing the **occupational health and safety** sector (€ 1.2 million).

The **1999 Cross-Border Cooperation Programme** consisted of the following main components

- expansion of the Kuressaare water and sewage network (€ 2 million)
- the Small Projects Fund (€ 1 million).

Under the **Large-scale Infrastructure Facility**, € 11 million was provided as Phare co-financing towards

- the Small Municipalities Environment Project (€ 6 million)
- the remediation of the Sillamäe radioactive tailings pond (€ 5 million).

Regarding **Phare programme management**, deconcentration of Phare from Headquarters to the Delegation took place on 15 December 1998. The National Programmes for 1996 and 1997 are implemented in a partly centralised and partly decentralised manner. The National Programmes from 1998 and 1999 are being implemented under a fully decentralised system.

The CFCU in the Ministry of Finance has managed the workload well during 1999, whereas the performance of line ministries has varied. In particular, horizontal coordination between ministries needs strengthening. Towards the end of 1999, the Ministry of Finance began to reorganise and strengthen the management of Phare. With the support of the CFCU, the National Fund (set up in 1999) supervised financial management and eased the transfer of funds to the final beneficiaries in Estonia.

The performance of the Phare Programme in terms of contracting and payments was generally satisfactory in 1999. About 13.5 per cent of the 1997 programme was contracted during December 1999, which was unnecessarily late. By the end of 1999, all 1990-1997 programmes were contracted (98.6 per cent of the 1997 programme was contracted). The contracting rate for the 1998 programme reached approximately 54 per cent at the end of 1999.

Results

In 1999 the Phare Programme achieved particularly positive results in the areas of education, regional development and SME development.

In the **educational** field, OMAS concluded its assessment of Phare programmes in support of education in Estonia in February 2000. The assessment noted the 'conspicuous' success of three Phare programmes: the Language Training Programme, the Vocational Education and Training Reform Programme and the Higher Education and Science Reform project.

Managed and implemented by the UNDP office in Estonia, the Language Training Programme set out to improve the situation for the Soviet-era immigrant population of Estonia in three major areas

- to make training in Estonian more accessible to the adult population (which includes easing access to Estonian citizenship)
- to improve the possibilities for youngsters to learn Estonian
- to ensure the availability of high-quality teaching materials to facilitate the integration process beyond the programme's duration.

Activities under the Vocational Education and Training Reform Programme (managed and implemented by the VET Reform Foundation) include the updating of vocational training curricula in the Estonian system. Three vocational training institutions are also being developed; additional benefit is derived from the location of these institutions in economically disadvantaged regions of the country.

Finally, under the Higher Education and Science Reform project (managed and implemented by the European Training Foundation), technological centres have been established and the higher education system internationalised. A significant contribution to the reform of higher education and science has been made through the establishment of Centres of Strategic Competence at Tartu and Tallinn Universities, focusing on gene technologies, information technology, environmental technologies and materials sciences. The Centres are functioning well, undertaking research projects involving a number of master and doctoral degree students, who may also benefit from career opportunities provided by numerous spin-off companies established by the universities.

Case study: Standards

In order to join the European Standards Organisation (CEN), Estonia must adopt 80 per cent of existing EN standards (numbering some 4,500 at end-1999). The Standards Programme (€ 1 million) has helped to facilitate this process. In 1999, the Phare Programme provided the Estonian Standards Board with a complete standards database, advice from Dansk Standard, terminology and translation support, a print-on-demand system for easy access to standards adopted and financing for building works (in order to house the new facilities).

The purpose of the programme was to make European standards available to Estonian industry and trade. To this end, the Estonian Standards Board received technical assistance for expert groups working with standards, the implementation process was furthered, a print-on-demand system was installed and the physical surroundings were renovated. At the conclusion of the programme, the Estonian Standards Board had a database with all EN standards documents in English and a considerable number partly accessible in Estonian.

Aided by relevant amendment to Estonian legislation (the Law on Technical Regulations and Standards was adopted in 1999), more than 1,000 EN standards had been officially adopted before the end of 1999. The legislative changes and Phare Standards Programme have laid the foundations for Estonia to become a full member of CEN by the end of 2002.

The 'Technical assistance for standards expert groups project' has achieved the following results

- the establishment of procedures for national Technical Committees
- the identification of the following fields as candidates for new Standards Committees: machinery, textile industry and piping systems
- the training of Technical Committee members
- the establishment of a database with all EN standards
- the identification of standards to be translated and adopted by cover page method
- the establishment of a prioritised schedule for translation work.

The 'Approximation of terminology project' has achieved the following results

- the establishment of a term database, containing approximately 8,700 Estonian terms from EN, IEC and ISO vocabulary
- the availability of 4,355 standards cover sheets in Estonian
- the training in terminology of EVS staff and Technical Committee members
- the submission of a development plan for the Term Database to the Ministry of Economic Affairs and Estonian Standards Board.

It should be noted that, for EU membership, Estonia also needs to join CENELEC and adopt its standards. The above programme is not sufficient to reach this additional target.

Hungary

The year in review

The overall performance of the Hungarian economy in 1999 was much better than thought possible in the middle of the year. With GDP growth of slightly more than 4 per cent (preliminary estimate), Hungary was one of the most dynamic economies in the region. The principal engine of growth was booming industrial exports, especially exports of multinationals settled in Hungary, while domestic consumption also started to recover. It seems that the continuous growth is not endangering the internal and external equilibrium and the inflation rate is also steadily decreasing. An important factor of the Hungarian success story is foreign direct investment, which did not stop after a peak in 1995; the total cumulative amount of FDI exceeds 22 € bn.

Overall, Hungary has made further progress on structural issues, particularly in the area of fiscal reform. Reform within the state-owned enterprise sector has continued but the pace of privatisation is inevitably slowing following the significant progress of previous years. A few large enterprises are still listed for privatisation and the state is holding some minority stakes. At the beginning of 1999, the privatisation agency held stakes in some 388 enterprises, 150 of which were undergoing bankruptcy proceedings. In May 1999, a 5.7 per cent minority stake in the telecommunications company MATAV was sold for € 300.2 million.

The 1999 budget law contains a number of improvements, such as the combined collection of tax and social security obligations. Over the medium-term, the government plans to reduce the tax burden on labour by cutting the marginal rates of personal income tax and by replacing general tax credits with specific ones. Initially, the rate of social security contributions was cut. On the expenditure side, means testing for family allowances was abolished and exemptions for higher education fees were reintroduced.

However, progress on health sector reform has been disappointing, while the government's decision not to increase contributions to the second pillar threatens the long-term viability of the new pension system. The mandatory contribution rate was left unchanged, even though the pension reform law envisaged a rise from 6 to 7 per cent.

While the former Minister of Economics, Chikán, was replaced by Mr Gyorgy Matolcsy in December, no substantial changes in economic policy are expected in 2000. However, the new Minister announced a Hungarian "New Deal", the *Széchenyi* plan, including large-scale house and road construction projects. With the improving economic outlook on main export markets, mainly in the EU, Hungary expects an accelerating growth of around 6 per cent in the coming years. While Hungary is increasingly seen more as a "converging market" rather than an "emerging market", some structural reforms (such as health care or public finance reform) are unlikely to be fully implemented during this government term.

As a result of the *1998 Parliamentary elections*, a coalition of three centre-right parties (FIDESz, FKgP, MDF) was set up under Prime Minister Viktor Orbán. The next general elections will be held in Hungary in 2002.

With regard to Parliament, some preparatory steps were taken to ensure minority representation in Parliament but no legislation on minority representation has yet been passed. The Government adopted a new development programme aimed at enhancing public administration in four main areas: development of regional public administration, decentralisation of tasks from national to regional level, modernisation of services and career development for civil servants. The judiciary continues to function satisfactorily.

In the area of foreign policy, Hungary continues to actively portray itself as a stabilising force in the region. Hungary became a member of NATO in March 1999 and can regard its first year of membership as very successful. Despite the obvious difficulties of its position, Hungary supported the NATO air campaign against the Federal Republic of Yugoslavia (FRY). In November 1998, Hungary took over the Presidency of the Council of Europe for six months. As concerns relations with the EU, accession negotiations were launched on 30 March 1998.

In July 1999, Hungary presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. The meetings of the Association Committee and Association Council were held in February and December 1999 respectively. The Joint Parliamentary Committee met once, in February 1999. 1999 also saw the publication of the second Regular Report (see box below) on Hungary's progress towards accession.

**Conclusion of the European Commission's Regular Report,
October 1999**

Hungary fulfils the Copenhagen political criteria. Two areas still need attention. The first is the situation of the Roma, where the government is beginning to implement its medium-term Roma action plan and needs to make available adequate budgetary resources. The second is the fight against corruption where recent efforts need to be reinforced.

Hungary is a functioning market economy and the legal and institutional structures which underpin the market economy have been further strengthened. It should be able to cope with competitive pressures and market forces within the Union in the medium-term, provided that it continues to make further progress in structural reforms.

Hungary continues to make progress in aligning and implementing the *acquis* in most sectors. Progress has continued regarding laws on public procurement and intellectual property, legislation on self-employment and the implementation of the new approach in the standards and certification areas. Progress is steady but slow in the agricultural, veterinary and phytosanitary fields. Alignment is well advanced in the transport sector, with the exception of the railways.

Further progress is required in the excise and audio-visual areas, labour and health and safety at work. Apart from the fight against organised crime, alignment has been slow in justice and home affairs, particularly with regard to border management and asylum, and there has been no progress in customs. There has been a slowdown in the adoption of environmental legislation.

Hungary has made steady progress in building up its administrative capacity to apply the *acquis*. Steps have been taken towards general public administration reform and most of the key institutions needed for implementation of the internal market are in place.

Hungary has satisfactorily addressed most of its short-term Accession Partnership priorities with the exception of administrative strengthening in regional development, steel sector restructuring and alignment in the environmental sector. Hungary has also made good progress in implementing the medium-term priorities.

Phare in 1999

In December 1999, the European Commission and the Hungarian authorities signed the financing memorandum for the 1999 Phare National Programme for Hungary, which amounted to € 91 million. In addition to this amount, the Phare Programme has also financed the continuation of the TEMPUS programme (2.181.034 € for 18 projects) and will further contribute to the opening of Community programmes (€ 12.6 million) through separate financing proposals.

The **1999 Phare National Programme** concentrates on several priorities. It finances efforts aimed at

- strengthening the **democratic system**, the rule of law, human rights and the protection of minorities, in particular the Roma; € 5 million has been allocated to the education of disadvantaged youth, with particular emphasis on the Roma
- reinforcing **institutional and administrative capacity** in the fields of financial services supervision, taxation, customs, agriculture and the environment (€ 35.2 million),
- providing support in the area of **economic reform**, including the promotion and development of SMEs (€ 6.2 million)
- assisting in the area of **justice and home affairs**, including the fight against organised and economic crime, border management and the strengthening of the judiciary (€ 13.6 million)
- supporting **infrastructure and transport investments** (€ 20 million), such as the reconstruction of the Esztergom-Stúrovo Bridge (Hungary/Slovakia) and the rehabilitation of the rail link Budapest Ferencváros-Soroksár
- developing **public health laboratories** (€ 8 million)
- supporting **end-users of programmes** (€ 3 million).

An additional € 17 million was allocated to the **cross-border cooperation (CBC)** programmes: € 10 million for cooperation with Austria, € 5 million for cooperation

with Romania and € 2 million for cooperation with Slovakia. Hungary also continues to participate in and benefit from Phare funded horizontal programmes such as TAIEX, Consensus III, the Small and Medium-sized Enterprises Facility and the Large Scale Infrastructure Facility.

Under the **Phare twinning** scheme, a total of 17 twinning projects for the 1997 and 1998 programmes got under way providing long-term assistance to: the agricultural sector (for developing the information system and planning capacity for the structural and agri-environmental development scheme); the public finance sector (for adapting the tax system and developing a monitoring system for state aid and foreign aid); justice and home affairs institutions (for the fight against crime, asylum and refugees, border management and training of law enforcement bodies). Furthermore, twinning assistance has been provided for preparing the operation of pre-accession aid (ISPA and SAPARD) and for institution building related to the development of testing and certification bodies and the market surveillance system. As regards the twinning projects for the 1999 programme, the Hungarian authorities have already chosen the Member State twinning partners and the twinning covenants will be submitted to the Commission soon.

Hungarian performance in **Phare programme management** has substantially improved during 1999. It was a particularly difficult year, since the contracting period of two annual Phare programmes expired during that year, the 1996 programme (on 30.9.1999) and the 1997 programme (on 31.12.1999). At the beginning of 1999, the commitment rate of both programmes was very low (20 per cent for 1996 and 5 per cent for 1997) and the Hungarian administration undertook substantial efforts to increase the overall contracting level. As a result, by the end of the contracting period, 98 per cent of the funds allocated had been committed.

The establishment of a National Fund and a Central Financing and Contracting Unit in December 1998 provided a good opportunity to tackle the implementation difficulties and improve crisis management. The Commission has stressed the need for the recruitment and training of skilled staff for these new structures.

Results

The Phare Programme has allocated € 1.030 million to Hungary during the period 1990-1999. Despite implementation difficulties, the achievements of the Phare Programme itself can be seen across a range of sectors.

In the field of **microcredits**, the Phare Microcredit Programme has assisted more than 10,000 small enterprises in the last seven years. One of the keys of the success of the programme, besides focusing on the individuals and providing advice, is regular monitoring: enterprises are from time to time re-examined even if they pay the instalments on time. The experience and know-how of the microcredit managers of the Local Enterprise Agency Network also contributed to good results. The microcredit scheme has thus contributed to the development of a healthy business environment and has helped to create jobs where most needed.

With regard to **training courses**, about 250-300 professionals working in the field of regional development are receiving basic and free training in project management

with special focus on EU requirements. This initiative of the PROMEI Modernisation and Euro-Atlantic Integration Project Office is being implemented by a consortium led by DHV Hungary.

Case study: Cross-Border Cooperation (CBC)

The Phare CBC programme helps promote cooperation between border regions of EU Member States and neighbouring candidate countries. It also aims at creating links between networks on both sides of borders and linking these in turn with wider European networks. In addition, the programme works to combat disparities in growth and living standards at EU external borders, to encourage conditions which favour political stability and has as its overall aim to help prepare Hungary for accession to the Union.

In 1999, several CBC programmes were ongoing

- the Trilateral Hungary-Slovakia-Austria programme, which had funding of € 1.5 million, including € 750,000 for Trilateral Agro-science Cooperation to the Agricultural University of Mosonmagyaróvár for modern conference and training facilities
- the Trilateral Hungary-Slovenia-Austria programme concerned the Trilateral Nature Park Development and aimed to facilitate transport between settlements in the southwestern part of Zala County and on the Slovene side of the border; bicycle paths were also developed within this framework
- the Bilateral Hungary-Romania programme covered several aspects of Hungarian/Romanian Cooperation, including setting up a European Documentation Centre and developing a curriculum for the study of European law; the programme also included the rehabilitation of the border crossing station at Csengersima, as well as environmental and nature protection, with particular emphasis on water management
- the Bilateral Hungary-Austria programme was particularly important in 1999; the cooperation between Hungary and Austria has been quite diverse in nature and the following main components were covered in 1999: Infrastructure; Economic Development and Cooperation; Human Resource Development; Environment and Nature Protection; projects included the construction of large-scale infrastructure (such as the Győr-Gönyű cargo port and the construction of several bypass roads), support for industrial parks, innovation and technology centres for SMEs and the construction of several waste depots to improve the environment.

The above shows the constructive support given to Hungary's pre-accession efforts by Phare funding. It is intended to continue to build on this experience in the years 2000-2006.

Latvia

The year in review

Economic activity in Latvia slowed considerably in 1999 as a result of the Russian crisis, with the reduction in trade links with Russia damaging some export sectors. Real GDP growth slowed towards the end of 1998 and economic output continued to contract in the first half of 1999, by 2.1 per cent year-on-year. The crisis led to a widening of external imbalances and to the emergence of a budget deficit. The banking sector was also affected, but stringent measures by the supervising authorities averted a systemic banking crisis. Overall, the Latvian authorities responded to the Russian crisis with an appropriate mix of policies and continued with the reform agenda. Despite the slowdown in the EU economy, Latvia continued to increase its exports to the EU.

Sectors oriented towards domestic activity continued to grow in 1999, but export-oriented sectors experienced a considerable slowdown. The transport and communications sectors contracted, agricultural output fell (mostly due to a decline in crop production), while food exports were also hit by the Russian crisis. The labour market was affected by the economic downturn and registered unemployment rose to 9.9 per cent by the end of July 1999.

From August 1998, exports to the CIS fell to half their previous level, while exports to the EU grew, but not enough to offset the reduction in exports to the east. As a result, the current account deficit almost doubled to 11.1 per cent of GDP, although the situation improved in the first quarter of 1999, with a narrowing of the trade and current account deficits to 11.7 per cent and 8.7 per cent of GDP respectively.

Inflation continued to fall in 1999 and, by August, 12-month inflation was down to 2.1 per cent compared to 3.5 per cent in September 1998. Monetary policy continued to focus on maintaining the fixed exchange rate peg to the Special Drawing Rights basket of currencies. In the summer of 1999, the lats came under pressure as markets became concerned about the size of the emerging budget deficit. The Bank of Latvia spent around € 38 million on intervention to support the lats while the government took measures to reduce the deficit.

Due to the general elections in autumn 1998, the 1999 budget was not adopted until February. The adopted budget was based on a growth forecast of 4 per cent in 1999 and aimed for a general government deficit of 2.8 per cent of GDP. As a result of the economic slowdown, revenues were well below forecasts while spending grew sharply, leading to a budget deficit. In order to limit the size of the deficit, the government issued a supplementary budget in August, cutting expenditure. The end-year deficit was expected to be around 3.5 per cent of GDP.

Structural reform in Latvia has advanced. The privatisation process is close to completion: by June 1999, privatisation regulations had been adopted for 18 of the remaining 41 enterprises. The government is committed to the sale of the remaining large state enterprises (Latvenergo, Lattelekom and the Latvian Shipping Company). Privatisation terms for the Latvian Shipping Company were agreed by the government on 17 August 1999.

The Latvian banking sector was hit hard by the Russian financial crisis in 1998, but the authorities acted swiftly to prevent the problems spreading through the sector. The sector began to show signs of recovery in the second quarter of 1999 - profitability improved and credit growth resumed. Consolidation of the banking sector continued and the legal framework for the financial sector was reinforced.

A number of changes have taken place in the government in Latvia. The centre-right minority government formed after the general elections in October 1998 signed a cooperation agreement with the Social Democrats in February 1999, who were allocated a ministerial post (agriculture) in the government. Presidential elections took place in June 1999; the new president (the first female president in Latvia) has no party affiliation. In July, the Prime Minister resigned and a new centre-right minority government was approved by parliament two weeks later.

There has been no major shift in government policy and EU and NATO membership are still key government objectives. Parliament adopted the law 'on the status of stateless persons' in February 1999. Latvian accession to the 1954 UN Convention relating to the status of stateless persons is under way and Parliament approved the relevant law in September 1999.

In June 1999, Latvia presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. The second meetings of the Association Council and Association Committee were held in February and June 1999 respectively. The Joint Parliamentary Committee met in January and October 1999. In 1998/1999 Latvia carried out a first Joint Assessment with the European Commission. 1999 also saw the publication of the second Regular Report (see box below) on Latvia's progress towards accession.

Conclusion of the European Commission's Regular Report, October 1999

Latvia fulfils the Copenhagen political criteria. Although significant progress has been achieved in the integration of non-citizens, it will be necessary to ensure that the final text of the Language Law is compatible with international standards and the Europe Agreement. Areas which still need attention are the strengthening of the judiciary and its efficiency, the reinforcement of the fight against corruption and the promotion of Latvian language learning among non-citizens.

Latvia can be regarded as a functioning market economy. It should be able to cope with competitive pressures within the Union in the medium-term, provided that it maintains macroeconomic stability and commits itself to completing structural reform.

Latvia has made important progress in further aligning its legislation with the internal market *acquis*, in particular as regards sector-specific legislation for the free movement of goods, free movement of services, competition and state aids. Competition and state aids authorities have become operational and function well.

Steady progress has been made in taxation, energy and rail transport. Important improvements can be noted in environment, in particular in environmental impact assessment and air quality. In the field of justice and home affairs, there have been positive developments, notably as regards visas and asylum.

Significant work remains to be done on intellectual and industrial property protection, data protection, company law, telecommunications, agriculture and fisheries, regional policy, financial control and the customs administration. Alignment and strategic planning in the environmental field needs to be translated into implementation and enforcement. Police capacity and the fight against organised crime have to be strengthened.

Latvia has continued to address the Accession Partnership short-term priorities in a satisfactory manner, demonstrating good progress in aligning its legislation with the *acquis* and in setting up the structures required to implement it in most areas. However, the delays in implementing general public administration reform have weakened capacity in this respect. The development of implementation and enforcement capacity needs to be addressed in a more systematic manner, with an emphasis on telecommunications, agriculture, customs and tax administration, maritime safety and financial control.

Phare in 1999

In 1999, the Latvian government and the European Commission signed the Financing Memorandum for the Phare National Programme for Latvia. A total of € 44.5 million was allocated to Latvia under the 1999 Phare budget to support Latvia's accession to the EU, in line with the priorities highlighted in the Accession Partnership.

Phare support for Latvia's accession preparation was channelled through four main programmes: the Phare National Programme (€ 14.2 million plus € 1.6 million for Latvia's participation in Community programmes), the Special Action for the Baltic Sea Region programme (€ 3 million), the Large-Scale Infrastructure Facility (€ 14.1 million) and the Catch-Up Facility (€ 7.955 million). Tempus has continued the activities of the successful Joint European Projects and of the Individual Mobility Grants in 1999 with an allocation of 296.502 € for 3 projects.

Latvia also participated in Phare multi-beneficiary and horizontal programmes in 1999, including Consensus III (€ 1.35 million) and the Project Preparation Facility 2000/01 (€ 2 million).

In line with accession priorities, the **1999 Phare National Programme** focused on the following

- acceleration of the **integration of non-citizens** into Latvian society (€ 0.5 million): improvement of language training for non-Latvian-speaking non-citizens
- reinforcement of **institutional and administrative capacity** (€ 2.4 million): State Revenue Service modernisation, Eurofaculty at the University of Latvia and capacity building for the CFCU

- further integration of Latvia into the **internal market** (€ 5 million): legal approximation, modernisation of food control at national and regional level and upgrading of the Latvian statistical information system
- **justice and home affairs** (€ 4.5 million): Latvian eastern border management and infrastructure
- **transport** (€ 1.8 million): Via Baltica reconstruction (Iecava-Bauska).

The 1999 **Baltic Cross Border cooperation** programme (€ 3 million) consisted of the following components

- development of sewage services in the Talsi municipality (€ 2 million)
- Small Projects Fund (€ 1 million).

Under the **Large-Scale Infrastructure Facility**, € 14.1 million was provided to Latvia as Phare co-financing towards

- three and five municipalities water services development (€ 5.5 million)
- Liepaja/Madona environment project/bolt-on (€ 6.6 million)
- ISPA project preparation support (€ 2 million).

Latvia was also allocated pre-accession support through the **Catch-Up Facility** (€ 7.955 million) in 1999, including

- improvement of the working environment in private and privatised enterprises (€ 2.05 million)
- energy sector restructuring (€ 3.105 million)
- prevention of corruption within the court system (€ 1.3 million)
- development of inter-ministerial cooperation for the prevention of corruption in governmental institutions (€ 1.5 million).

In addition to the above commitments, a range of programmes and projects were launched in 1999 and projects from previous years were continued or completed.

In **justice and home affairs**, analytical equipment was procured for the forensic science laboratories (€ 250,000) and technical assistance was provided. Two twinning projects also began: 'Court System Reform' (€ 600,000), led by the German Ministry of Justice, provides assistance in the drafting of legislation and in the creation of a statistics database, a Judicial Cooperation unit within the Ministry of Justice and a training programme for judges in European law. The Finnish Ministry of Interior is providing expert assistance and training to the Latvian Border Guard (€ 1 million), covering all aspects of border management, from legislative analysis and the Schengen Information System through to patrolling and dog training.

In the **transport sector**, the Phare Programme provided technical assistance to the Ministry of Transport and support for the improvement of road, rail and marine infrastructures. A project on 'Traffic Safety in Iecava' was completed during the year. Reconstruction works on bridges over the Memele and Gauja rivers began and a feasibility study for a bridge and tunnel under the Daugava River in Riga was launched. Regarding marine infrastructure, the construction of the Vessel Traffic Services Central Tower in Riga was completed in 1999.

In the **energy sector**, the Energy Efficiency Fund began to allocate loans in 1999 through the Latvian Development Agency and the Mortgage and Land Bank. The total Phare donation to the Fund for the year amounted to € 1 million.

In the field of **environment**, the Ministry of Environmental Protection and Regional Development received extensive technical assistance. During 1999, the Latvian Environmental Investment Fund received support to build staff capacity to manage the funds provided by Phare (€ 2 million) and other donors.

Within the framework of the **Cross-Border Cooperation Programme**, water management projects were started in Cesis (€ 900,000), Sigulda and Limbazi (€ 772,054), Ainazi and Saulkrasti (€ 1.025 million). Financing was also provided to purchase laboratory equipment in several environmental sectors (around € 800,000).

Under the **LSIF programme**, technical assistance was provided for the preparation of ISPA projects (around € 1 million). The LSIF is also providing financing for water management projects in ten Latvian cities (€ 12.1 million).

In the area of **European integration**, direct support for strengthening the European Integration Bureau (EIB) and the inter-ministerial accession preparation process was provided through a second phase of the 'European Integration Programme' (€ 1 million). Targeted support was also provided to the Latvian Parliament (Saeima).

In 1999, three large-scale projects in the **agricultural sector** came to an end. At the central level, a € 1.8 million project supported the Ministry of Agriculture in its preparation for the CAP. Around 20 'junior experts' were employed and trained on all aspects of the CAP. In the area of rural development, support was provided to the 'diversification of the rural economy' (€ 1.2 million), providing practical experience in a number of pilot regions. In October 1999, a cross-sectoral project on food control was completed, which supported cooperation between the Ministry of Agriculture and the Ministry of Welfare. As one of the first twinning projects, German and French experts began work with the Ministry of Agriculture in autumn 1999, to mobilise and transfer Member States' experience in the veterinary and phytosanitary field and in land use policy.

In the **economic and financial sectors**, a project supporting the Ministry of Finance and the State Treasury (for around € 2.5 million) was finalised. The Foreign Direct Investment and Economic Development project (for around € 1.64 million) enabled the Latvian Development Agency to establish good cooperation between the investors and the various administrations involved.

Phare provided extensive support to the **Ministry of Welfare**. Forty primary health care practices were equipped with medical equipment and 20 practices with office equipment. In another project, theoretical training for primary health care doctors was provided and training programmes for postgraduates were prepared.

Support continued for Phase II of the **Latvian language training** programme, a multi-donor programme administered by the UNDP. The programme aims to provide language training to both language teachers and teachers in minority schools, who now have to teach subjects in Latvian in line with the new Education Law. The

Naturalisation Board in Latvia has benefited from the purchase of technical equipment in order to create an automated system for the maintenance of the naturalisation process (24 000€).

Implementation of the Phare Programme in Latvia improved considerably in 1999. The programmes are implemented under the Decentralised Implementation System. The CFCU increased efficiency in managing and implementing the various programmes. The National Fund was set up and became fully operational in May 1999. Two other Implementing Agencies were set up for investment support programmes. The National Fund supervises the financial management of the various programmes.

The performance of the Phare Programme in terms of contracting and payments has substantially improved. By the end of 1999, all 1990-1997 programmes were fully contracted. The contracting rate for the 1998 programme reached approximately 40 per cent at the end of 1999. The overall disbursement rate in 1999 reached 70 per cent.

Results

Substantial progress has been made in the approximation of Latvian legislation with the EU *acquis*. The pace and quality of the approximation process has been helped considerably by a number of Phare technical assistance projects which have provided expert guidance on the drafting of legislation across a number of sectors.

A large-scale project (**Approximation of Latvian Legislation**), with a budget of € 4 million, was successfully implemented throughout 1999 and came to an end in December. The project delivered substantial assistance to line ministries and the European Integration Bureau (EIB). It assisted in drafting specific laws and assessing Latvia's progress in law approximation in order to help develop EIB's database; training for staff within each line ministry was delivered and support provided for the Legal Department of Parliament. In total, the scope of the project covered 929 EU legal acts across all sectors.

Technical assistance provided by Phare in the **economic and financial sectors** contributed to the institutional strengthening of several institutions in 1999, including the tax administration, State Treasury and Latvian Development Agency. Concrete results have been achieved through a number of projects.

For example, the 'Technical Assistance to the Tax Sector in Latvia' project has contributed significantly towards ensuring that Latvia meets a number of essential requirements in the area of taxation. Application of the tax law and the harmonisation of VAT have been particularly successful. Regarding excise tax, progress has been made in the harmonisation of the three existing laws (on tobacco, alcoholic beverages and mineral oil products) with EU Directives. Amendments to the existing legislation on income tax have improved the applicability of that tax. Organisational structures have also been enhanced by the strengthening of tax audit procedures. Finally, staff know-how in the areas of tax audit and the application of VAT law has been upgraded.

Case study: Institution building in occupational health and safety

This has been one of the most successful institution building projects at the Ministry of Welfare. The Ministry of Welfare Department of Labour (DoL) and the State Labour Inspectorate (SLI) were under government orders to proceed urgently with approximating the occupational health and safety (OSH) legislation and increasing administrative capacity to apply the *acquis*.

The project has contributed to the development of strategy and to the drafting of an Action Plan on meeting the OSH *acquis* at the Ministry. One of the key outputs is that the Latvian draft Law on Labour Protection is fully compatible with the EU Framework Directive. The administrative, organisational and financial consequences for the SLI in assisting in implementing the OSH provisions were assessed and recommendations made, together with the foundation of a rating system to determine the visit patterns of SLI inspectors. Other components supported the development of computerised rating systems. The project initiated a new definition of the role of labour inspectors, who should move from a policing role to an advisory one.

Lithuania

The year in review

Lithuania experienced an economic downturn in 1999, mainly caused by the disruption of trade relations with Russia following the Russian financial crisis in 1998. Unemployment rose and inflation fell to very low levels, partly because products meant for export flooded the domestic market. Structural reforms progressed, but in some important sectors, such as energy, they remained incomplete.

In the first quarter of 1999, real GDP dropped by 5.7 per cent year-on-year, due to the slowdown of external demand and to an interruption of oil supplies to the Lithuanian oil refineries, which makes up a significant share of industrial output. In the first five months of 1999, industrial sales were 7.6 per cent lower than in the same period of 1998.

In the first half of 1999, total exports declined by 23.4 per cent, due to a decrease in exports to the CIS of over 60 per cent, and imports declined by 19.4 per cent. In the first quarter of 1999 the trade deficit stood at 11 per cent of GDP and the current account deficit at 10 per cent of GDP. During the first five months of the year, Lithuania's foreign debt rose by more than one-fifth in nominal terms, after having remained unchanged during most of 1998.

The average registered unemployment rate rose to 7.9 per cent in the first seven months of 1999, up from 6.6 per cent in the corresponding period of 1998. Inflation fell drastically, due to the appreciation of the litas, surplus agricultural goods on the domestic market and global trends in commodity prices. In August 1999, 12-month inflation was 0.2 per cent, compared to 3.6 per cent in September 1998. Excise taxes and some regulated prices were raised, but falling food prices, which account for some 40 per cent of the consumer price index, offset any inflationary pressure.

The Lithuanian authorities had planned a balanced budget for 1999, based on an optimistic growth forecast of 4 per cent. However, when revenues and expenditures missed their target by 10 per cent in mid-year, the new government had to take corrective measures. The transfer of the final round of the Savings Restitution Plan (returning lost savings to households) was postponed and expenditure in the budget was due to be cut by 6 per cent. Full implementation of these measures could bring the financial deficit down to around 5 per cent in 1999.

Structural reforms moved forward in 1999, notably with the partial privatisation of the Lithuanian Telecom Company. During the first nine months of 1999, privatisation revenues accounted for about 1.3 per cent of GDP (five times higher than 1998). The privatisation list still contains 2,500 enterprises with public shares to be privatised. 242 enterprises were due to be privatised before the end of 1999, with the Mazeikiai refinery being the most important one. In the financial sector, the largest insurance company was successfully privatised and the two remaining public commercial banks were listed for privatisation.

In the budgetary area, the authorities increased excise rates on alcohol, tobacco and fuel products, with the final goal of reaching the minimum rates set in the EU. Budgetary procedures were modified: programme budgeting was introduced and a five-year work programme for the consolidation of all budget funds at the national and municipal level was established.

In the banking sector, several foreign institutions opened local branches and offices. In May 1999, the Bank of Lithuania formulated merger and acquisition rules as banking sector consolidation continued. Hermis Bankas bought Industrias Bankas and opened negotiations with Vilniaus Bankas, the largest private bank. This merger was approved by the Bank of Lithuania in September.

Private sector involvement in the energy industry increased with the acquisition of a minority stake in the Lithuanian Electricity Company by a foreign company. However, a project to link the Lithuanian and Polish electricity networks fell through.

Land restitution continued but is not yet complete. As of April 1999, private ownership was restored for 59 per cent of all land for which claims were made. The government has made a financial commitment to complete restitution of the existing claims by 2006. The purchase of non-agricultural land by foreign entities is now allowed.

With regard to political developments, the government resigned at the beginning of May 1999 and a new government took office on 10 June, after obtaining the confidence of the Parliament (Seimas). The new government has confirmed Lithuania's commitment to accession to the EU. The next parliamentary elections will take place in autumn 2000.

Lithuania continues to make progress in the field of public administration. In July 1999, the Seimas approved a new Law on the Civil Service which aims to ensure the independence of civil servants and improve the efficiency of the public administration. Lithuania ratified the European Charter of Local Self Government in June 1999. Regarding the judiciary, Lithuania has made substantial progress in cutting the excessive length of court proceedings, caused by a lack of qualified staff and organisational problems and thus has reduced the backlog of court cases.

In June 1999 Lithuania presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. Association Council and Association Committee meetings were held in February and June 1999 respectively. The Joint Parliamentary Committee met in February 1999. 1999 also saw the publication of the second Regular Report (see box below) on Lithuania's progress towards accession.

Conclusion of the European Commission's Regular Report, October 1999

Lithuania fulfils the Copenhagen political criteria. Areas which still need attention are the fight against corruption and the continued reform of the judiciary.

Lithuania has continued to make progress in establishing a functioning market economy and is on the way to being able to cope with competitive pressures and market forces within the Union in the medium-term, provided it completes the remaining reform agenda.

Lithuania has made progress in most areas of the internal market, in particular in public procurement, intellectual and industrial property, conformity assessment, free movement of capital and services and anti-trust legislation. Further efforts are needed in the areas of state aids control and the free movement of goods. No progress has been made in the audio-visual sector and major efforts are required to bring taxation into line with the *acquis*.

Sustained effort is needed in the agricultural sector and much remains to be done on fisheries. While progress is good in transport, efforts should now focus on fiscal harmonisation in road transport, maritime safety and the aviation *acquis*. Despite significant progress in the environmental field, the level of compliance is uneven. Much remains to be done on regional policy and little progress has been made on financial control. There has been great progress in justice and home affairs, but little in customs.

Lithuania has made determined efforts in the field of energy policy and has taken a welcome decision on the closure of the Ignalina nuclear power plant, which represents a significant sign of its commitment towards European integration.

Continued attention is needed to ensure that the progress made in transposing the *acquis* and in meeting most of the short-term Accession Partnership priorities is matched by similar progress in strengthening implementation and enforcement capacity. Particular attention should be paid to state aid control, environment, customs, regional policy, financial control and social policy. The new public administration law and the continued reform of the judiciary are positive developments in this respect.

Phare in 1999

On 17 December 1999, the Lithuanian government signed the Financing Memorandum for the Phare National Programme for Lithuania. A total of € 66.7 million was allocated to Lithuania under the 1999 Phare budget to support Lithuania's accession to the EU, in line with the priorities highlighted in the Accession Partnership.

Phare support for Lithuania's accession preparations was channelled through four main programmes: the Phare National Programme (with a budget of € 26.9 million), the Cross-Border Cooperation Programme (€ 3 million), the Large-Scale Infrastructure Facility (€ 14.4 million) and the Catch-up Facility (€ 7.5 million). € 2 million was allocated to a Project Preparation Facility. Lithuania also participated in Phare multi-beneficiary and horizontal programmes in 1999, including Community Programmes and the Anti-Drug, Transport, Customs, CREDO, Common Policy, Consensus and Baltic Sea Region programmes. Tempus has continued the activities of the successful Joint European Projects and of the Individual Mobility Grants in 1999 with an allocation of 194.777 € for 2 projects.

€ 10 million was allocated to support projects linked to the forthcoming closure of Unit 1 of the Ignalina Nuclear Power Plant. This is the first instalment of a financial assistance package worth around € 150 million.

In line with accession priorities, the **1999 Phare National Programme** focused on

- strengthening the **public administration** (€ 4 million)
- **internal market** (€ 3.5 million)
- **justice and home affairs** (€ 6 million)
- **agriculture** (€ 4.5 million)
- **energy** (€ 3.25 million)
- **social affairs** (€ 2 million)
- **environment** (€ 2.5 million).

The **1999 Cross-Border Cooperation Programme** consisted of the following main components

- Panemune border crossing (€ 2 million)
- Baltic Projects Facility (€ 1 million).

Under the **Large-Scale Infrastructure Facility**, € 14.4 million was provided as Phare co-financing towards

- Klaipeda and Panevezys waste water treatment plants (€ 10.2 million)
- ISPA Project Preparation Facility (€ 2.2 million)
- Jurbarkas waste water treatment plant (€ 2 million).

Lithuania also received pre-accession support through the **Catch-Up Facility** in 1999, for

- the Lithuanian Property Development Fund (€ 5 million)
- the fight against Corruption (€ 2.5 million).

A number of **earlier programmes** were also completed during the year.

From the CBC Programme, the Tourism Information Centre in Nida was extended and is now equipped with state-of-the-art interpretation and presentation conference facilities. Phare financed the necessary construction works and the equipping of the Conference Centre, which is also intended to bring visitors to Nida outside the peak holiday season.

The Lithuanian Metrology Institute received assistance through a Phare project worth around € 2 million. This project enables the Institute to use modern calibration equipment and reference materials and to replace the standards system originating from the Soviet era by standards used throughout the EU.

The registration centre for foreigners has been modernised with a Phare grant of around € 650,000. In addition to the improvement of sanitary facilities within an existing building, a completely new building designed to accommodate up to 200 people has been constructed.

The 1996 project 'Pre-SPP institutional strengthening to support an integrated structural and cohesion-type development programme' (in preparation for the Structural Funds) helped to draft a strategic planning document, which was then developed into the first National Development Plan for Lithuania. The project ended in October 1999 and was followed by the launch of the first SPP activities (twinning and Klaipeda urban pilot project) in December 1999. Furthermore, in the field of regional development, the 1997 project 'Regional Development and Development of Local Government' and the ongoing project 'Regional Development' have both helped to lay the foundations for regional policy activities in target regions.

The first three **twinning** projects started in 1999. The National Standardisation Bureau and the National Accreditation Office are being strengthened with the support of Sweden and Germany; a training programme for the border police and the customs administration is being carried out by Finland; Finland is also leading a project to help prepare Lithuania for management of the Structural Funds (SPP).

To a large extent, **implementation of Phare programmes** focused on the contracting of 1997 programme funds. More than 92 per cent of these were contracted before the end of 1999. The introduction of the Decentralised Implementation System and a fully operational CFCU helped to speed up contracting.

Results

Major achievements, after some years of substantial investment, were seen in the **environmental sector**, with the inauguration of biological treatment at the Kaunas waste water treatment plant in September 1999 and at Palanga in November 1999. Two major 'black spots' in the environmental sector were thus removed or substantially reduced.

In the **health sector**, the focus on primary health care delivered good results. Starting in 1995, the Phare Programme has contributed to the preparation and implementation of a Primary Health Care Plan. Five Primary Health Care Centres have been inaugurated, the last of which opened in 1999. The Centres are located in Siauliai region, Klaipeda city, Klaipeda region, Vilnius city and Vilnius region. Given the success of this programme, a follow-up scheme has been agreed, which will come to an end in 2000; however, this time the main beneficiaries will be private general practitioners rather than Primary Health Care Centres.

Case study: Upgrading of Food Control

In Lithuania, various government agencies involved in different aspects of food control need to be better coordinated, in order to avoid duplication of tasks and to facilitate a more effective food control system. In addition, the existing system of food certification needs to be fundamentally changed, in order to harmonise it with EU requirements.

These issues were addressed by the contractor F+U (from Heidelberg Germany) in a € 2 million project. The project also provided support to upgrade the analytical capacity of the National Veterinary Laboratory of the State Veterinary Service, through the procurement and supply of equipment, in order to strengthen the existing infrastructure of food control in Lithuania.

In addition, staff were trained and food legislation was developed in line with EU food law. Finally, regional and central laboratories were linked to border inspection points. The latter activity will be followed up by the construction and equipping of veterinary and phytosanitary border inspection posts under Phare 1998-2000 along the future EU external border of Lithuania with Belarus and Russia (Kaliningrad region).

The project ended in May 1999.

Poland

The year in review

The Russian crisis induced a slowdown from the high rates of economic growth that Poland had experienced over the previous three years. Industrial production and domestic demand fell in early 1999 and unemployment rose briefly above 12 per cent in March. However, there were signs of a resumption in growth later in the year; industrial sales recovered to 5 per cent year-on-year in the second quarter of 1999.

Poland's current account deficit continued to widen, from 4.3 per cent of GDP in 1998 to over 6 per cent in 1999. Over the first half of 1999, exports continued to be lower than in 1998, mainly due to a decrease of more than two-thirds to Russia, but the impact on the trade deficit was limited as imports also dropped. In the first six months of the year, the current account deficit of € 4.5 billion remained to be covered by capital inflows, including over € 2 billion of FDI. The slowdown in economic growth and the reduction in interest rates made the Polish economy less attractive to international investors and foreign reserves declined each month until July, when they were boosted by inflows from privatisation and the appreciation of the Euro.

Inflation decreased to 5.6 per cent in March 1999, compared with an annual average of 11.8 per cent in 1998, but then rose above 6 per cent on a year-on-year basis. This mainly reflected the depreciation of the zloty in the first four months of the year, by some 15 per cent against the US dollar and the Euro. The fall in inflation and the fast recovery of the zloty in the aftermath of the Russian crisis allowed a series of interest rate cuts. However, real rates remained high as inflation expectations failed to subside.

The Polish authorities are gradually implementing the privatisation programme adopted in July 1998, which envisages that 44 enterprises will remain in public ownership. Privatisation over the period to 2001 should cover more than 70 per cent of the assets held by the state and raise more than € 35 billion. The sale of around 70 firms in 1999 is expected to contribute € 3.6 billion to government revenue.

Following the sale of 15 per cent of the shares of TPSA, the national telecoms company, in 1998, a further 40 per cent of shares were due to be sold by the end of 1999. Advisers were selected for the privatisation of LOT airlines, the Polish petroleum, mining, gas and spirits industries, as well as a coal mine and several heat and power generating plants. Polish State Railways was restructured into separate infrastructure, passenger transport and freight sections to prepare it for privatisation. Substantial progress was made in privatising banks, with the sale of a 52 per cent stake in Pekao Bank and an 80 per cent stake in Zachodny Bank in June 1999, to foreign strategic investors. About 60 per cent of total assets in the banking sector are now in foreign hands.

The exposure of the banking sector to Russia was very limited. In addition, the ratio of non-performing loans to total assets fell for the fifth year in a row, to below 10 per cent. Financial markets deepened and market capitalisation of the stock exchange rose substantially. Implementation of the pension reform from April 1999 onwards should

boost the development of Poland's capital markets, as the establishment of pension funds will enhance domestic demand for financial instruments.

In June 1999, the government agreed to a significant reform of the tax system, with focus on simplifying the system, lowering tax rates, broadening the tax base and removing incentives to 'grey' activities. There will be a gradual reduction in the corporate tax rate to 22 per cent in 2003; income tax deductions will be removed in 2000 and income tax rates will be reduced in 2001.

The coalition government has exercised its mandate in a democratic fashion. Poland's political institutions continue to function properly, including ongoing 'cohabitation' between the executive and the president. The government continues to support EU membership as a top political priority. Poland's accession to NATO on 12 March 1999 underlines the government's commitment to integration into Euro-Atlantic structures. During 1999, the government has focused on a domestic reform process designed to modernise many areas of society. Reforms have been undertaken in the areas of health, education, social security and regional administration.

A new administrative structure at central, regional and local level entered into force on 1 January 1999. This devolves powers to three levels of self-government (voivodships, poviats, gminas) and reduces the number of voivodships from 49 to 16. Further reforms of the functioning of the state administration were envisaged in the Act on Governmental Departments, which was adopted on 1 April 1999 and which should lead to a smoother running of the Executive. The revised 1998 law on the civil service entered into force on 1 July 1999 and aims to establish an open and competitive career system. With regard to the judiciary, little progress has been made and the limited development of the judiciary and its administrative capacity remain a source of concern.

In May 1999, Poland presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. Association Council and Association Committee meetings were held in December and April 1999 respectively. The Joint Parliamentary Committee met in March 1999. 1999 also saw the publication of the second Regular Report (see box below) on Poland's progress towards accession.

**Conclusion of the European Commission's Regular Report,
October 1999**

Poland fulfils the Copenhagen political criteria. Further efforts are necessary to increase the efficiency of the judiciary. Attention should be paid to the fight against corruption.

Poland is a functioning market economy, with an increasingly thriving private sector and an appropriate legal and institutional environment for economic activity. It should be able to cope with competitive pressures and market forces within the Union in the medium-term, provided that it keeps up the pace of economic restructuring and proceeds with trade liberalisation.

Poland's track record in the areas of free movement of services and capital is good. Although alignment needs to be pursued in the area of public procurement and competition, there are indications that effectiveness has increased. However, there has been little progress in the areas of industrial and intellectual property, data protection, conformity assessment and certification and state aids.

Clear strategies for steel restructuring and the automobile sector are still needed. Although progress has been made in the veterinary and phytosanitary *acquis*, the cost of implementation has not been adequately budgeted. Poland has not yet launched the transformation that is needed - in terms of policy, *acquis* and structures - in the agricultural and fisheries sectors.

Some progress has been made in the energy sector. In the environmental field, framework legislation has not been transposed and an implementation programme, financial strategy and effective monitoring are still required. Good progress has been made in transport alignment, but efforts have been limited in the social field. The legal framework and related structures for regional administration still need to be established.

Progress has been made in customs, but more effort is needed on alignment, implementation and financial control. Some progress has been made in justice and home affairs (notably border guards), but alignment remains limited and law enforcement bodies and judiciary capacity need to be reinforced.

Overall, Poland has not progressed significantly in aligning its legislation and in adapting and strengthening the structures required in a large-sized country in preparation for accession. In the same manner, Poland has addressed the Accession Partnership short-term priorities only to a limited extent, with a notable lack of progress on certification, state aids and steel restructuring. Continued efforts are needed to set up or strengthen capacities in intellectual property protection, certification, state aids, agriculture and regional policy, the social field, customs and justice and home affairs.

Phare in 1999

On 31 December 1999, the Polish Government and the European Commission signed the Financing Memorandum for the Phare National Programme for Poland.

A total of € 302.1 million was allocated to Poland under the 1999 Phare budget to support Poland's accession to the EU, in line with the priorities highlighted in the Accession Partnership.

Phare support for Poland's accession preparations was channelled through three main programmes: the Phare National Programme (with a budget of € 230.5 million), the Cross-Border Cooperation Programme (€ 38 million) and the Large-Scale Infrastructure Facility (€ 33.6 million). Poland also participated in Phare multi-beneficiary and horizontal programmes in 1999.

In line with accession priorities, the **1999 Phare National Programme** focused on

- **economic reform and industrial restructuring** (€ 31 million)
- **institutional and administrative capacity** (€ 38 million)
- **internal market** (€ 10.4 million)
- **agriculture** (€ 27.55 million)
- **environment** (€ 26.2 million)
- **transport** (€ 64 million)
- **regional policy and cohesion** (12.15 million)
- participation in **Community and other programmes**, including Tempus (€ 21.2 million).

The **1999 Cross-Border Cooperation Programme** consisted of the following main components

- Cross-Border Cooperation Programme Poland-Germany (€ 32 million), comprising projects with a cross-border impact in transport (€ 15.5 million) and the environment (€ 12.3 million) and a small projects/small infrastructure fund (€ 4.2 million)
- Cross-Border Cooperation Programme Poland-Czech Republic (€ 3 million), comprising one environmental project and a small projects fund with cross-border impact
- special action in favour of the Baltic Sea Region (€ 3 million), comprising one environmental project and a small projects fund with cross-border impact.

Under the **Large Scale Infrastructure Facility**, € 33.6 million was provided as Phare co-financing towards an ISPA project preparation facility (€ 6.6 million), three environmental projects (€ 22.5 million) and a Phare project preparation facility (€ 4.5 million).

Twinning has become the core of institution building in Poland. A total of nine twinning projects are currently being implemented and are devoted to institution building in four key areas, namely agriculture, environment, justice and home affairs and preparation for structural funds; coal and steel restructuring is also being assisted through twinning.

Implementation of the Phare Programme in Poland is through the Decentralised Implementation System but the in-country administrative structure was reorganised significantly in 1999, with the creation of a CFCU, the establishment of the National Fund at the Ministry of Finance, the creation of a limited number of Implementing Agencies and the phasing out of the old PMU system.

The performance of the Phare Programme in terms of contracting and payments was satisfactory in 1999. By the end of 1999, all 1990-1997 programmes were fully contracted. The contracting rate for the 1998 programme amounted to 48 per cent at the end of 1999. Total contracting amounted to € 218 million in 1999 and the rate of contracting at the end of 1999 stood at 79 per cent of all funds allocated to Poland over the 1990-1999 period. Disbursements amounted to € 183 million.

Results

Phare also achieved positive results in a number of key sectors during 1999.

In the **transport sector**, Phare has made a major contribution to the improvement of Poland's road network, notably with the construction of the Katowice bypass (€ 35 million) and the Poznan bypass (€ 45 million). These are located on the A4 motorway (Trans-European Corridor III) and the A2 motorway (Corridor II) respectively and aim to link Berlin with Kiev and Moscow. The Phare-funded project for the supply of rails and upgrading of the Berlin-Warsaw-Minsk railway line on Polish territory was completed in 1999.

A project to alleviate the social effects of **coal and steel restructuring** in Poland has been under way since 1998. This project should be seen in the context of the Polish government's plans to restructure the coal and steel sectors and to lay off more than 150,000 workers over a period of five years. The project is conditional on the government's commitment to the continued restructuring and privatisation of the steel sector in Poland, which is one of the main priorities of the Accession Partnership. In this context, Phare funding is being provided for SME development, together with temporary income support, retraining and counselling for workers laid off.

Regarding **cross-border cooperation**, a number of Phare-funded projects that aimed to improve border crossings along the Polish-German border were completed in 1999. A number of environmental and municipal infrastructure projects were also completed.

Building on the **STRUDER regional development programme** of previous years, Phare continued to fund small-scale municipal infrastructure development in the least developed regions of Poland in 1999. A total of 95 small infrastructure projects were completed in these regions, targeted mainly at upgrading municipal water supply networks, waste water treatment plants and roads, as well as at establishing local business incubators to encourage SME development.

In 1999, as part of ongoing Phare funding regarding regional policy and cohesion, the Polish Government completed the preliminary **National Development Plan** and was able to provide preliminary draft Operational Programmes for five selected voivodships (provinces) of Poland.

A Phare-funded **export promotion** programme was completed in 1999, together with an **SME development** programme.

In the field of **agriculture**, Phare continued to support the harmonisation of Polish legislation with the *acquis* in 1999. As far as investment is concerned, Phare activities concentrated on the purchase of equipment for dairy cooperatives, the upgrading of the milk reference laboratory and support for the development of wholesale markets.

Environmental projects in 1999 focused mainly on air protection, waste treatment, maritime waste treatment and the protection of bio-diversity in the Elk area through the construction of a waste water treatment plant.

Phare projects in the area of **justice and home affairs** concentrated on the eastern border, with € 13 million going towards the training of border guards, the police and migration officers in addition to the procurement of equipment for mobility, tactical support and telecommunications development for the police and border guards. In addition, two roads were constructed on the Polish-Ukrainian and Polish-Belorussian borders.

Case Study: Twinning project: ‘Strengthening of the Public Prosecutors Office in fighting organised crime and the reform of the justice system’

Launched by Phare in 1998, twinning is proving to be an effective instrument in the reform and strengthening of the justice system in Poland.

This twinning project, with France as the lead twinning partner and Germany and the Netherlands as junior partners, is undertaking training for judges and officials within the judiciary. It aims to help modernise the penitentiary system and implement the reform of Poland’s court system. At the same time, the project is promoting international judicial cooperation. The project is also training public prosecutors in EU law and the fight against organised crime and will help to strengthen the judiciary by developing modern IT systems. A National School for Judges is also being set up.

The project will cost € 6 million (Phare: € 3 million; Polish Government: € 3 million) and will last for three years.

Romania

The year in review

Romania's economic situation has remained fragile. The poor economic performance has been caused by an inappropriate macroeconomic policy mix, the slow pace of restructuring of large state-owned enterprises and a resulting lack of confidence in the economy. In 1999, however, structural reforms were stepped up, allowing the authorities to reach agreement with the international financial institutions on a new structural adjustment programme. As a result of this agreement, substantial additional support has been mobilised for the restructuring process.

Real GDP continued its downward trend, falling by 3.9 per cent in the first half of 1999. The large fall in output led to an increase in the registered unemployment rate from 9 per cent in October 1998 to 11.3 per cent in July 1999. In early 1999, the precarious balance of payments situation raised doubts about Romania's ability to service its large external debt on time. Speculative pressures caused a sharp fall in the currency in March. However, the authorities stabilised the currency and repaid all of their external debt obligations on time.

In the autumn of 1998, the National Bank of Romania abandoned its policy of ensuring some real exchange rate appreciation to support the fight against inflation. The leu was allowed to depreciate in real terms and lost almost two-thirds of its nominal value between October 1998 and June 1999. This strong depreciation rekindled inflation, which grew from 32.5 per cent in February to 49.5 per cent in August 1999 on a year-on-year basis.

Fiscal policy continued to accommodate the lack of structural reforms. The accumulation of tax arrears had negative consequences on the budget and the shift from direct to indirect taxation reduced revenues. Parliament approved an austerity budget in early 1999, but implementation proved difficult and the state budget deficit was 40 per cent higher than the planned annual deficit in August 1999. Interest charges became the largest expenditure item, accounting for 32 per cent of total spending at the end of June 1999.

Privatisation accelerated, particularly for large enterprises, with 68 companies sold in the first eight months of 1999. More contracts were concluded with foreign investors and more sales were carried out on the capital markets. The sale of SMEs also accelerated. However, overall performance remained disappointing: many tenders failed to generate interest or had to be cancelled, including an important deal for the largest oil refinery.

Two small public banks were sold to foreign investors in late 1998 and spring 1999 and the government started privatisation procedures for two other large public banks. Following a liquidity crisis, the largest public bank, Bancorex, was taken over by the National Bank of Romania. The bad assets of Bancorex were transferred to an Asset Resolution Agency and, at the end of July, Bancorex was closed.

In late 1998, the government presented a structural reform plan designed to reduce the losses in the economy by 30 per cent, through the closure or restructuring of large loss-making enterprises. However, while some progress was made in the restructuring of mining enterprises and in downsizing many public companies, the problems of some of the largest loss-makers were not addressed.

Little progress has been made on key fiscal reforms. The government introduced measures to improve tax collection, in particular by inducing taxpayers to settle their debts and not to accumulate new arrears. A new law enables ministries to take control of highly indebted companies through a special 'debt for equity swap'. Finally, the government has initiated a programme to reduce arrears at the three largest utility providers.

Romania still has to design structural reforms to control public spending in the medium-term, including the overhaul of the health and social security systems and the reform of the tax structure. Progress in these areas has been mixed. Health insurance houses were created and a new global income tax system was due to enter into force on 1 January 2000. However, in the area of pension reform, the government has not yet implemented a new multi-pillar system to replace the current pay-as-you-go scheme.

Progress has been made in the restructuring of agriculture, notably in the context of the agriculture structural adjustment loan agreed with the World Bank. External tariffs were lowered and privatisation of grain trading and storage companies was accelerated. However, the privatisation of state farms has been blocked due to continuing legal problems.

Deterioration in socio-economic conditions resulted in a number of episodes of civil unrest. When the miners carried out violent demonstrations and attempted to march from Jiu Valley to Bucharest in January, the government dealt with public order while respecting the right to strike and demonstrate. There was also a serious deterioration in the conditions of children in care in 1999, due to a combination of economic, financial and administrative factors.

The government passed an increased number of ordinances in 1999. Although the government is permitted to legislate by ordinances, their increased use is worrying because it mixes the legislative and executive powers. There can also be considerable delay before ordinances are ratified, modified or even rejected by Parliament. The Law on the Liability of Ministers was promulgated in June 1999, clarifying the status of members of government. However, the civil service law has still not been adopted. Finally, measures have been taken to strengthen the working of the judiciary.

On 18 June 1999, the Supreme Defence Council adopted a new National Security Strategy, in which membership of the EU was identified as a core priority. In the same month, Romania presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. Association Council and Association Committee meetings were held in April and September 1999 respectively. The Joint Parliamentary Committee met in April 1999. 1999 also saw the publication of the second Regular Report (see box below) on Romania's progress towards accession.

**Conclusion of the European Commission's Regular Report,
October 1999**

The Commission considers that, at the moment, Romania still fulfils the Copenhagen political criteria although this position will need to be re-examined if the authorities do not continue to give priority to dealing with the crisis in their child care institutions. The Commission will monitor recent decisions by the government to provide the resources and carry out reforms which put child care on a secure basis, with full respect for human rights.

Further measures are needed to ensure the independence and efficiency of the judiciary. Other areas which still need attention include the fight against corruption and the situation of the Roma. Romania cannot yet be considered as a functioning market economy and is not able to cope with competitive pressures and market forces within the Union in the medium-term.

The government is committed to addressing the structural problems in the economy. Priority should be given to improving financial discipline and restructuring loss-making enterprises. Macroeconomic stabilisation should be accompanied by the creation of a more business-friendly environment in order to develop economic activity and build on the considerable potential of the Romanian economy.

Alignment in the internal market area is only partial and Romania needs to step up transposition and implementation in this area. Significant progress was made with the adoption of a law on public procurement, as well as in the banking sector and in the area of financial control. Some progress was made in standards and certification but the lack of framework legislation is impeding progress. The bankruptcy laws have been amended but not aligned.

The adoption of a new law on state aid control and the transformation of the regiés autonomes into public companies were important developments. There has been some progress in agriculture, although land registration remains slow. There is a need to further align veterinary controls and upgrade the agri-food industry. There has been significant progress in legislative alignment in the transport sector, but maritime and road safety need more attention. There are continuing problems in the air, water and waste management sectors. There has been progress in justice and border management, the police and immigration, but work is needed on asylum and drugs control.

Lack of funds and weak administrative capacity continue to cause problems. Public administration reform has not started in earnest; some key institutions need to be set up and major efforts are needed in many sectors to upgrade the level of competence. The independence of regulatory and supervisory bodies, including the Central Bank, needs to be ensured.

While Romania has addressed certain aspects of administrative capacity and the internal market, both short-term priorities of the Accession Partnership, certain aspects of justice and home affairs and environmental priorities have not been satisfactorily addressed.

Phare in 1999

In 1999, the Phare Programme for Romania aimed at providing support to help Romania prepare for accession to the EU. Phare support for Romania's accession preparations was channelled through seven main programmes: the Industrial Restructuring and Employment Conversion Programme (€ 100 million), the Phare National Programme (€ 55.2 million), the Catch-up Facility (€ 21 million), the Large-Scale Infrastructure Facility (€ 14.3 million), the Project Preparation Facility (€ 3.5 million), the Cross-Border Cooperation Programme with Bulgaria (€ 5 million) and the Cross-Border Cooperation Programme with Hungary (€ 5 million). Romania's participation in Community programmes was supported by a Phare allocation of € 8.7 million in 1999 and an allocation of € 2.592.543 million was provided for the Tempus programme (23 projects).

The **Industrial Restructuring and Employment Conversion Programme (RICOP)** provides support to mitigate the consequences of industrial restructuring in loss-making state enterprises identified in the context of the conditionality of World Bank and IMF programmes for Romania. Support is focused on locations where severe job losses are expected. € 100 million has been made available for a number of measures, including severance pay, advisory services to workers, active employment measures and retraining, public works, development of social services and SMEs.

The **1999 Phare National Programme** for Romania covered support for

- strengthening the **Romanian judicial system** and developing **child welfare** services
- supporting projects in the areas of **standardisation and conformity** assessment, **competition and state aids** and acceleration of **privatisation**
- strengthening **border management**, supporting **pre-accession impact** studies, supporting the institutional strengthening of the **Ministry of Finance**, controlling **money laundering**, strengthening **maritime safety** and improving **health and safety at work**
- elaborating a National Action Plan on **Employment**.

Support from the **1999 Catch-up Facility** was divided between

- preparation for the privatisation of the Constanta oil terminal
- management of environmental liabilities in the context of the privatisation of state-owned oil refineries
- assistance for the modernisation and restructuring of Romanian railways
- implementation of a restructuring plan for the Romanian national airline
- a programme to support the fight against public corruption and organised crime.

Romania's participation in the **Large-Scale Infrastructure Facility** (part V) covered four projects

- extension and modernisation of the Mangalia (Constanta region) waste water treatment plant
- the Jiu Valley waste water treatment station
- a regional water and environment project for the Municipality of Brasov
- a thermal energy conservation project (Oltenita).

The **1999 Project Preparation Facility** helped to prepare projects for implementation in the context of regional development programmes and the National Development Plan.

The **1999 Cross-border Cooperation Programme** with Bulgaria covered, on the Romanian side, the modernisation of the gas pipeline crossing the common border, rehabilitation and safety work on the Giurgiu-Ruse bridge and the establishment of a joint air-quality monitoring system on the lower Danube. The 1999 Cross-border Cooperation Programme with Hungary covered, on the Romanian side, the development of the cargo air terminal at Arad and flood prevention in the upstream river Tisa basin.

The National Agency for **Regional Development** also became operational on 1 January 1999. Its success in supporting the establishment of regional development authorities in Romania's eight macro regions is one of the significant achievements of 1999, enabling Romania to start its preparations for the management of structural funds.

Under **twinning**, 15 covenants between Romanian institutions and Member State authorities were endorsed by the Delegation during 1999 and the benefits of this new approach began to be felt.

The **implementation** of projects under previous Phare programmes continued in 1999. Contracts totalling € 161 million were concluded during the year, compared with € 87.20 million in 1998, reflecting improved programme management by the Romanian authorities and increased efficiency achieved through deconcentrating responsibility for Phare procedures to the Commission's Delegation.

A new management and financial system was successfully introduced in 1999. This required the establishment of a National Fund in the Ministry of Finance. The National Fund supervises the implementation of programmes by a limited number of Implementing Agencies, which are integral parts of the national administration. This streamlining had already been anticipated by the establishment of a single CFCU in 1998. The CFCU had an important impact on the implementation of Phare programmes in 1999. The amount committed by the CFCU in 1999 was € 46.346 million (37 contracts) compared to € 6.884 million in 1998. The advantages of having a strong, specialised contracting unit in the Ministry of Finance are now being felt.

Results

Significant results were achieved in various areas that benefited from Phare assistance in 1999.

The **SME Development Programme** is a continuation of a series of projects that benefited from Phare support under the 1994 Phare budget. The objectives of the programme were to strengthen the capacity of the Romanian banks to extend medium-term credits to SMEs and to effectively implement a pilot credit scheme. Both components of the programme have performed well. Three local banks have been selected by tender to implement the pilot credit scheme, which got under way in June 1999. The selected banks established their implementing capacity and 19 SME focal

points were successfully created by the banks. The Agency for SMEs, acting as Implementing Authority, developed its own software to monitor the implementation of the pilot scheme.

In cooperation with the EBRD and the EU, the government has developed a technical cooperation and investment programme for the rehabilitation of municipal water and waste water infrastructure, the **Municipal Utilities Development Programme**, MUDP II, with a total value of € 141 million. The MUDP II is targeting 10 towns (Arad, Bacau, Botosani, Bistrita, Braila, Cluj, Constanta, Focasani, Oradea and Targoviste). Phare support amounts to € 33.7 million, of which € 27.5 million is for investments and € 6.2 million is for technical assistance. These investments are helping Romania to meet the EU *acquis* in the area of drinking water and waste water and to gain experience in managing complex investment projects at local level. MUDP II is having a direct impact in terms of improved public water supply and waste-water infrastructure, while the technical assistance is helping transform the existing water utilities into efficient modern operators. The experience gained in the programme will be invaluable in view of the future investments required in this sector and in view of the launch of the new ISPA instrument in 2000.

The **Health Care Financing Reform Programme** (€ 4 million) was fully contracted in 1999. The major components of the programme are institutional reform, the reform of health sector financing and harmonisation of legislation in the pharmaceutical sector. The Phare contribution is supporting the development of a general concept of the health care system, approval of the 'Action Plan for the reform of the health care system', improvement of administration and management capacities at the central and district level and the development of new structures for the hospital sector. An analysis was carried out of the need for heavy medical equipment and assistance was provided for harmonising legislation in the pharmaceutical sector.

Progress was made in strengthening institutional reform in the **cultural sector**. This programme has two major objectives: (a) institutional development of the sector, with special focus on three areas: legislation, reform of the Ministry and support for local and regional authorities; (b) the setting up of a Fund for the development of arts and civil society, including industry-related projects emphasising the role of culture in inter-community relations. A new strategy for the Ministry of Culture with an appropriate training programme was elaborated and a consortium selected to manage the Cultural Fund (the British Council and the Civil Society Development Foundation). The first call for proposals will be launched at the beginning of 2000.

Case study: EU assistance to job creation in Gorj County and the Jiu Valley

The 'Assistance to Job Creation in Gorj County and the Jiu Valley' pilot project, which started in 1998, was under full implementation during 1999. The scheme had a total budget of € 850,000 and aimed at developing private SMEs, to promote regeneration and economic development in the coal mining regions of the Jiu Valley and Gorj County and alleviate the effect of restructuring the mining industry on employment in the regions.

The selection of the projects was carried out in two stages: (1) pre-selection of projects from the 257 projects submitted following a publicity and awareness campaign in the two regions; (2) assistance for the pre-selected projects (from Phare-funded consultants) in developing their business plans and detailed proposals. Representatives of both central and local government were involved in the selection process. A total number of 29 projects were selected for support, 15 in Gorj County and 14 in the Jiu Valley. Individual grants of up to € 70,000 were given for each project.

By the end of 1999, more than 650 new jobs had been created and, as a result, the same number of formerly unemployed people in the regions had found sustainable jobs. Some examples of successful businesses created within this project are

- in Gorj County: a car service and repair workshop in Targu-Jiu (€ 20,000 Phare support; 14 new jobs created); a farm in the Targu-Jiu suburban area (€ 67,000, 20 jobs created); an electrical motor repair workshop in Rovinari (€ 20,000, 25 jobs created); a dairy farm in Novaci (€ 7,400, 12 jobs created);
- in the Jiu Valley (Hunedoara County): a PVC double-glazing units production facility in Petrosani (€ 70,000, 30 new jobs created); a turning and machine workshop in Petrila (€ 50,000, 20 jobs created); a production unit in Petrosani for custom-made furniture and double glazing units in wood, aluminium and PVC (€ 12,000, 15 jobs created).

Slovakia

The year in review

The current Slovak government inherited very difficult economic conditions from its predecessor. The government's economic policies are a clear break from the past and the reform effort has been considerable. To restore macroeconomic stability, the government is cutting back the government deficit and re-launching the restructuring and privatisation of banks, enterprises and public utilities. Slovakia is currently experiencing a slowdown in economic growth as a result of these austerity measures.

Real GDP growth was just 2.4 per cent in the first half of 1999. The reluctance of the international financial markets to fund emerging markets with poor reform records after the Russian crisis has made it difficult for Slovakia to attract foreign financing. The ability of Slovak companies to raise foreign loans and refinance existing foreign currency debt has been particularly affected. As a result of the slowdown in growth, the unemployment rate jumped from 12.5 per cent in the last quarter of 1998 to 15.8 per cent in the second quarter of 1999.

Following record trade and current account deficits in 1998, the government introduced austerity measures in 1999, which are slowing down domestic demand and import growth. Because exports continued to grow by almost 10 per cent, the trade deficit decreased to about 6 per cent of GDP. A new 7 per cent import surcharge (June 1999) helped to dampen import growth. Foreign direct investment weakened in the first months of 1999, although it was expected to increase with the planned sales to foreign investors of parts of some of the larger enterprises and banks.

Having fallen in 1998, the inflation rate increased to 14.4 per cent in August 1999. The National Bank of Slovakia expected headline inflation to be between 13.5 and 15.5 per cent at the end of 1999. By May 1999, the Slovak currency (koruna) had depreciated by 14 per cent against the Euro since its floating in October 1998. Confidence in the koruna was restored after the government began to introduce additional fiscal and structural reforms and, by the end of September, the total depreciation against the Euro had declined to around 6 per cent.

In order to reduce the general government deficit, the government initially introduced short-term stabilisation methods, such as a freeze on public sector wages, cuts in public investment, increases in VAT and excise duties and measures to stabilise the financial situation in the health sector. Later in the year, these were complemented by measures that will have a more structural, medium-term impact on the budget, such as cuts in public employment and social security expenditure. Government estimates put the general government deficit at 2.4 per cent of GDP for the first half of 1999.

The government is working on a structural reform programme, including bank restructuring and privatisation, a workout scheme for non-performing loans, an overhaul of the legal and regulatory framework and the design of a regulatory framework for public utilities, followed by their commercialisation. The government is also checking the legality of non-transparent privatisation deals done in the past,

announcing that any shares returned to the state as a result will be re-privatised in a transparent manner.

The government abolished the Act on Strategic Enterprises, which had prevented the privatisation of so-called strategic enterprises, which included the public utilities, post and telecommunications, the railways, the financial sector, pharmaceuticals, agro-industry and the armaments and machinery sectors. With the approval of the Law on large-scale privatisation, these can now be privatised, while up to 49 per cent of the energy utilities can be sold. The government also launched the privatisation of part of the Slovak Telecommunications Company.

In August 1999, the government agreed the steps for restructuring and privatising state-owned banks before the end of 2000. By replacing the top management of the state-owned banks, the government is changing the policy of these banks. They are reducing their operational costs to prepare for privatisation and are actively trying to recuperate outstanding bad loans. However, they will need to be recapitalised, the budgetary cost of which might run to 1.2 per cent of GDP annually.

Numerous legal obstacles and conflicts between different pieces of legislation have hindered restructuring in Slovakia in the past. The government has identified the changes needed to the legal framework to promote enterprise restructuring and these were under preparation during 1999. The government announced that all legal amendments should be approved by Parliament before the end of 1999.

Driven by the EU membership objective, important developments have positively changed the political landscape in Slovakia. The Slovak Constitution was amended to allow for presidential elections by universal suffrage and direct presidential elections took place in May. Mr Schuster was elected for a five-year mandate, with 57 per cent of the vote and the support of the ruling coalition. Voter turnout was 75 per cent. The President was inaugurated in June; he visited the European Commission and NATO in July and confirmed Slovakia's commitment to join the EU.

The powers of the Slovak Parliament are respected and the opposition plays a full part in its activities. Despite diverging views on some key issues, the four-party coalition government has stayed together since the 1998 elections, showing its capacity to compromise and move the legislative agenda forward. The Slovak government has taken steps to strengthen the independence of the judiciary: a new law will lay down the rights, obligations and legal responsibilities of judges.

In May 1999, Slovakia presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. Association Council and Association Committee meetings were held in April and January 1999 respectively. The Joint Parliamentary Committee also met in January. 1999 also saw the publication of the second Regular Report (see box below) on Slovakia's progress towards accession.

Conclusion of the European Commission's Regular Report, October 1999

Thanks to the changes introduced since September 1998 Slovakia, now fulfils the Copenhagen criteria. The independence of the judiciary has improved *de facto* but needs to be consolidated *de jure*, notably through an amendment to the constitution eliminating the probation period for judges and modifying nomination and removal procedures.

Continued efforts are needed to sustain the stable functioning of democratic institutions, step up the fight against crime and corruption and protect minority rights. Particular attention needs to be paid to improving the situation of the Roma and to fighting discriminatory attitudes in society.

Slovakia is close to being a functioning market economy thanks to the policy decisions and reform agenda of the new government. Implementation of these decisions in the coming year should complete the legal and economic conditions of a functioning market economy. Continued progress towards sustainable macroeconomic stability and the implementation of the structural reform programme should enable Slovakia to cope with competitive pressures and market forces within the Union in the medium-term.

Slovakia has made important progress in legislative alignment in the internal market. A public procurement law was adopted, as was framework legislation in the areas of standards and certification. In the competition area, the law on enterprise revitalisation was abolished and state aids law was adopted. In the energy sector, there was commitment to closure dates for the Bohunice nuclear reactors. Some progress has been made in the banking and financial services area to improve transparency and protect minority shareholders.

In other sectors of the *acquis*, although policy decisions are moving the process in the right direction, there has been little progress in terms of adopted legislation. In the environmental field, the bulk of transposition of the *acquis* remains to be carried out. In justice and home affairs, much still needs to be done in amending the aliens and asylum laws and in fighting organised crime and corruption. Alignment on transport legislation is lagging behind and concrete actions are needed on regional development. Little progress has been made in the agricultural, veterinary and plant health fields and in the area of health and safety at work.

With regard to administrative capacity, coordination on EU policy matters has improved. However, the much-needed civil service reform law has not been adopted. In other areas, such as regional development, financial control and justice and home affairs, the establishment of relevant institutions has been delayed. Slovakia needs to accelerate its efforts in preparing laws and developing implementation and enforcement capacities.

Slovakia has adequately addressed the political, state aid and internal market short-term Accession Partnership priorities. However, insufficient attention has been paid to developing administrative capacity and aligning with the environmental *acquis*.

Phare in 1999

On 2 November 1999, the Slovak Government and the European Commission signed the Financing Memorandum for the Phare National Programme for the Slovak Republic.

The **1999 Phare National Programme**, with an allocation of 69.5 M€, included the following priorities

- strengthening of **civil society** and policies and institutions protecting the rights of minorities (4.3 M€)
- **export development** and initiatives to attract foreign direct investment, promotion of **SME development**, further equity contribution to the **Post-Privatisation** fund (SPPF) and continued support for the reform of the **cadastre** (26.7 M€)
- enhanced 'competitiveness', concerning **standards and certification, state aids and public procurement** (4.4 M€)
- further development and strengthening of **justice and home affairs** institutions, with focus on border management and migration control, the fight against organised crime and corruption and the development of capacity to handle asylum and legal and illegal migration questions, notably in view of the Schengen *acquis* (10 M€)
- alignment with and implementation of the **agricultural acquis** (4 M€)
- alignment of **agricultural statistics** (2 M€)
- development of **environmental monitoring and implementation** control structures and capacities, continuous planning and implementation of approximation programmes (1.5 M€)
- the implementation of a comprehensive **energy** strategy in line with the *acquis* (1.2 M€)
- reinforcement of **institutional and administrative capacity** in the field of customs, indirect taxation, telecom, safety and health at work, as well as the development of a public administration strategy and support to the CFCU (10.4 M€)
- **reconstruction of the Maria Valeria bridge** between Šturovo and Esztergom (5 M€).

The **1999 Cross-Border Cooperation Programme** includes the following components

- Slovak Republic/Austria programme (€ 4 million), focusing on projects aimed at improving environmental conditions through the reduction of air and water pollution
- Slovak Republic/Czech Republic programme (€ 2 million), aimed specifically at improving the quality of surface and underground water in the city of Skalica and neighbouring villages
- Slovak Republic/Hungary programme (€ 2 million), aimed at modernising the wastewater treatment plant in Lucenec.

In the framework of the **1999 Catch-up Facility**, Slovakia received an allocation of € 2 million to support activities for the Roma minority.

Further to the above allocations, € 4 million, 1.68 million and 1.73 million were also committed for TEMPUS, Community programmes (Education) and the Fifth Framework Research and Technological Development Programme respectively. The Slovak Republic also participated in Phare multi-beneficiary and horizontal programmes in 1999, including TAIEX (approximation of EU legislation), Consensus (social), Justice and Home Affairs and the SME Facility.

Finally, € 10 million was allocated for the 'Support of the **Decommissioning of Nuclear Power Plants** and Consequential Measures in the Energy Sector in Central European Partner Countries with Non-Upgradable Nuclear Reactors for the Slovak Republic'.

The performance of **Phare programme management**, in terms of contracting and disbursement rates, has continued to improve. By the end of 1999, all 1990-1997 programmes were fully contracted. The contracting rate of the 1998 Programme reached approximately 40 per cent at the end of 1998.

The Central Finance and Contracting Unit (CFCU), set-up at the end of 1997, has enabled the implementation of Phare assistance to be rationalised and streamlined, while ensuring sound financial management and effectiveness. As in the other candidate countries, a National Fund has been established in the Ministry of Finance. The latter supervises the financial management of Phare financed projects and is responsible for financial reporting to the European Commission.

Results

In 1999, the first **twinning** schemes (involving the secondment of Pre-Accession Advisers from EU Member States) were implemented. In this respect, some key Ministries in sectors of high priority for European integration were identified: Agriculture, Finance, Justice, Interior and Environment.

In 1999, in the field of **legal approximation**, a lawyers' consortium continued to provide the Slovak Government with advice on a whole spectrum of issues in this domain, supported by a central translation unit which provides translations of Community Law into the Slovak language (set up at the Institute of Approximation of Law in cooperation with TAIEX).

To foster the development of **civic society**, the Phare funded Civil Society Development Foundation (CDSF) continued to support NGOs in the fields of democracy, minorities, human rights, social activities and environment.

The **SME programme** continued to make a key contribution to the strengthening of the Slovak market economy and its competitiveness. The SME sector plays a dynamic role in stimulating economic growth and providing new opportunities for the labour force in Slovakia. The number of SMEs has steadily grown since 1991 and, in 1999, the SME share was approximately 58 per cent of GDP. In terms of employment, SMEs now contribute to approximately 60 per cent of total employment.

The Phare Programme has played an instrumental role in supporting this development of SMEs, both in terms of providing direct support to SMEs (both technical and

financial support) as well as creating sustainable institutions that provide services to SMEs. Since 1991, the PHARE programme has supported the SME sector with a total amount of over € 40 million, including the 11 million allocated under the 1999 National Programme. Together with government support, Phare helped establish the National Agency for SME Development (NADSME) and a regional network of 12 Regional Advisory and Information Centres (RAICs) and 5 Business Innovation Centres (BICs). Between 1995 and 1999, the network provided counselling services to more than 30,000 clients and developed/assessed 5,523 business plans, while 8,985 starting and existing SMEs were trained in 649 various courses. The activities of RAICs/BICs favoured the establishment of 2,447 new enterprises and assisted in the creation/maintenance of more than 15,000 jobs.

In terms of financial support, Phare provides a range of instruments (seed capital, guarantee, micro loans) of which the Phare SME Loan Scheme is particularly worth mentioning. This subsidised loan scheme provides a unique blend of Phare, government and commercial funding, thereby making available much needed capital to SMEs at favourable rates.

In the framework of the **export development programme**, Phare has supported the transfer of market oriented capabilities into the marketing know-how of Slovak producers: providing *inter alia* up-to-date and practical market information to enable enterprises take full advantage of opportunities in export markets; supporting the export development and promotion initiatives of individual firms through an export development investment scheme; encouraging the development of selected industrial sectors, by undertaking a series of comprehensive programmes, combining market, product and company development; financing promotional activities aimed at encouraging foreign buyers to source supplies from Slovakia.

The Export Development Investment Scheme (EDIS) has been particularly successful in providing financial support to Slovak exporters - manufacturers and trading companies - for investment in marketing, export technology and product development activities. The aim of the EDIS Scheme is to strengthen the marketing development skills, technological capabilities and the commercial competence of Slovak exporting manufacturers. Support is provided on a cost-sharing basis, up to a maximum of 50 per cent. The scheme also helps to increase awareness of the impact of marketing activities on export growth.

In the **environmental field**, the Environmental Grant Scheme has provided grant support to capital investment projects in the private and public sectors which directly facilitate compliance levels in key environmental problem areas, including: the construction and upgrading of systems for collecting, sorting, processing and disposing of hazardous and municipal waste; the construction and upgrading of drinking water supply systems, waste water supply systems and waste water treatment plants; the construction and upgrading of facilities for the reduction of air pollution; the introduction of integrated environmentally friendly technologies to prevent pollution at source as well as to promote waste reduction, to facilitate compliance with the EU's Integrated Pollution Prevention and Control directive.

Case study: LSIF - bypass construction

This project is financed through the “*1998 Large Scale Infrastructure Facility*” which has three specific objectives

- to facilitate priority investments in transport and environment with a significant accession and transboundary impact
- to facilitate loans from participating International Financial Institutions and co-financing from the beneficiary countries
- to familiarise the applicant countries with the competitive application and selection process - and the decentralised implementation procedures - which will be used by the Instrument for Structural Pre-Accession (ISPA).

The objective of the project is to build a 6.5 km section of the D-61 motorway to bypass the city of Bratislava. The project is located on Pan-European Corridor No. VI.

The new link will divert transit traffic and part of the urban through-traffic away from congested city centre streets, thus improving traffic conditions, safety and environmental conditions in the city centre. It is expected that the new motorway section will have an ADT (average daily traffic) of 19,000 to 25,000 vehicles per day, 15 per cent of which will be heavy vehicles

This project is co-financed by the European Investment Bank (a loan of € 72 million was signed for the completion of this project in December 1997), by Phare (€ 15 million) and by the Slovak State budget.

Slovenia

The year in review

The macroeconomic situation in Slovenia has remained favourable since mid-1998. Economic growth has slowed somewhat, but inflation has been reduced and export performance has been strong. The reform process has been reinvigorated by the adoption of new legislation. Much progress has been made in reforming the financial sector, notably with the adoption of laws on banking and foreign exchange. Value added tax was introduced in July 1999 and agreement on pension reform was reached between the government, employers and trade unions in May. Measures to remove some restrictions on capital inflows have been taken.

There was a continued slowdown in economic growth in 1999, with the real GDP growth rate declining to under 3 per cent in the spring. There has been no improvement in the labour market situation: the high share of long-term unemployed, the poor qualifications of the unemployed and the mismatch between labour supply and demand skills suggest that unemployment in Slovenia is mainly of a structural nature.

Slovenia remained relatively sheltered from the Russian crisis thanks to the earlier reorientation of its trade towards EU markets. However, the slowdown in growth in Germany and Italy, Slovenia's two main trading partners, was expected to result in a deterioration of the external accounts in 1999. Foreign direct investment inflows had slowed during 1998 (totalling € 148 million); this trend continued in 1999, with FDI inflows reaching just € 24 million for the period January-July.

The downward trend in inflation continued in 1999, with the year-on-year inflation rate declining from 6.5 per cent in December 1998 to 7.9 per cent in June 1999. Disinflationary pressures resulted from the real appreciation of the currency, the fall in import prices, moderate wage growth and increased competition on the domestic market, partly due to price liberalisation. The introduction of value added tax in July was expected to push inflation up in the second half of 1999.

With the privatisation of socially owned enterprises completed in November 1998, the government turned its attention to the financial institutions. In April 1999, the government authorised the management of two state banks to draw up privatisation plans. The privatisation of these banks, which account for 40 per cent of the market, is expected to take place over several years. As a first step, the state was expected to reduce its share in the Nova Ljubljanska Bank from 93 per cent in 1998 to 65 per cent in 1999.

The government, employers and trade unions reached agreement on the reform of the pension system in May 1999. This formed the basis for legislation which was expected to be adopted by Parliament before the end of 1999. Along with measures to improve the financial prospects of the pay-as-you-go system, the Draft Law on Pension and Disability Insurance foresees the introduction of a voluntary pension insurance scheme.

Value added tax was introduced in July 1999, replacing the existing sales tax. The new laws on VAT and excise duties are critical in aligning Slovenia's tax legislation with EU requirements. The VAT yield should compensate for the lower revenues from customs duties and pension contributions and for the withdrawal of the sales tax. The inflationary impact of VAT's introduction is expected to be short-lived. Most importantly, the wage policy agreement for 1999-2001 reached between the social partners will help to limit the impact of higher prices on wages.

Major steps have been taken to increase the competitiveness of the banking sector. The cartel agreement on maximum interest rates on deposits, which limited competition between the banks, ended in March 1999. The new Banking Law (January 1999) aims to open the sector to foreign competition, by allowing branches of foreign banks to be set up. The Banking Law also improves the regulatory and supervisory system in line with EU directives. The new Securities Market Law (June 1999) regulates brokerage and the stock market and allows the establishment of branches of foreign brokerage houses, while the Foreign Exchange Law (March) aims to liberalise capital flows in accordance with the Europe Agreement.

The centre-right government formed in 1997 is still in place with a coalition between the Liberal Democrats, the Slovene People's Party and the Pensioners' Party. There were four ministerial changes in the government, but these have not resulted in any major shift in government policy and EU membership remains a key objective. Slovenia has seriously addressed the weaknesses underlined in the 1998 Regular Report in order to reduce the delay in transposition of legislation in preparation for EU accession.

The legislative process continues to be slow: laws need three 'readings' in Parliament and coalition instabilities slow down Parliamentary decision-making. In March 1999, measures were adopted to facilitate a faster adoption of laws, according to the plan set out in the NPAA. Public administration reform is ongoing: the government decided to employ a further 247 civil servants in 1999, although not all posts have been filled as yet. The judicial process still remains slow; although the government has taken measures to reduce the delays and backlog, the number of pending cases is still high.

In May 1999, Slovenia presented a revised NPAA, in which it outlined its strategy for accession, including how to achieve the priorities of the Accession Partnership. Association Council and Association Committee meetings were held in February and March 1999 respectively. The Joint Parliamentary Committee met in March. 1999 also saw the publication of the second Regular Report (see box below) on Slovenia's progress towards accession.

Conclusion of the European Commission's Regular Report, October 1999

Slovenia fulfils the Copenhagen political criteria. Two areas which still need attention are the streamlining and speeding up of the judicial and parliamentary process.

Slovenia can be regarded as a functioning market economy. It should be able to cope with competitive pressures and market forces within the Union in the medium-term, provided that it continues to make further progress on structural reforms.

Slovenia has significantly accelerated its overall legislative approximation effort and demonstrated impressive progress across most sectors of the *acquis*. Key parts of internal market legislation have been adopted, for example in the areas of standards and certification, data protection, anti-trust and VAT/excise. The Customs Law has also amended. Progress has been made in capital liberalisation and the banking and security sectors. In justice and home affairs, laws have been passed on foreigners and asylum and measures taken to fight organised crime and corruption. In the environmental field, laws have been adopted in the fields of water, air, waste management and nature protection. Progress is being made in the veterinary and plant health fields, but there is still much to do in the agricultural sector.

Slovenia still needs to put the legal framework for state aids in place. Alignment needs to be completed on the free movement of persons, capital and services and border control and the fight against drugs need further attention. Efforts are needed to align public procurement and intellectual and industrial property law. No progress has been made on aligning audio-visual legislation.

Slovenia has made little progress in general public administration and judicial reform. The sectoral legislation that has been adopted provides for the establishment of many of the necessary structures: these institutions now need to be set up and adequately staffed. Steps have been taken to consolidate institutional capacity in the competition, employment and social affairs, agricultural and customs areas, but attention needs to be paid to strengthening the environment, taxation, state aids and justice and home affairs administrations. Supervisory and regulatory authorities need to be established for public procurement, energy and telecommunications.

Slovenia has met many of its short-term Accession Partnership priorities. Internal market legislation has been adopted, measures have been taken to clarify property legislation, progress is being made in transposition in the environmental field and recently adopted legislation provides for many of the institutions needed to implement the *acquis*. However, short-term Accession Partnership priorities have only been partially met in the areas of banking and insurance and administrative and judicial capacity (adoption of a civil service law, land registration, financial control).

Phare in 1999

On 23 December 1999, the Slovene Government and the European Commission signed the Financing Memorandum for the Phare National Programme for Slovenia.

A total of € 63 million was allocated to Slovenia under the 1999 Phare budget to support Slovenia's accession to the EU, in line with the priorities highlighted in the Accession Partnership. This amount includes the annual allocation of 1999 plus the carry-over from 1998, granted by the Commission.

Phare support for Slovenia's accession preparations was channelled through the following programmes: the Phare National Programme (with a budget of € 27 million), the Cross-Border Cooperation Programmes with Italy (€ 5 million) and Austria (€ 2 million), the Large-Scale Infrastructure Facility (€ 21 million), the participation to the community programmes (€ 2.75 million) plus the national allocation of multi-beneficiary and horizontal programmes (€ 5.25 million).

Slovenia also participated in other Phare multi-beneficiary and horizontal programmes in 1999, including the programmes on Information, Small Projects, Justice and Home Affairs, Statistics, Business Support, Evaluation, TAIEX and Nuclear Safety.

In line with accession priorities, the **1999 Phare National Programme** focused on

- reinforcement of **capacity to adopt and apply the *acquis*** (€ 8 million)
- further integration of Slovenia into the **internal market** (€ 3.33 million)
- **economic and social cohesion** (€ 10.77 million)
- **justice and home affairs** (€ 4.9 million).

The **1999 Cross-Border Cooperation Programme** consisted of the following main components

- Cross-Border Cooperation with Italy (€ 5 million): pollution prevention in the Gulf of Trieste and regional development structures in the Slovene-Italian border region
- Cross-Border Cooperation with Austria (€ 2 million): development of a biomass district heating system and a Small Projects Fund.

Under the **Large-Scale Infrastructure Facility**, € 21 million was provided as Phare co-financing towards

- LSIF Part III - Maribor Waste Water Project - Bolt-on (€ 6.5 million)
- LSIF project preparation support (€ 2 million)
- LSIF Part V - Kranjska Gora waste water project and Murska Sobota railway project (€ 12.5 million).

A national allocation for the following multi-country and horizontal programmes was granted to Slovenia: Tempus II (€ 1.25 million), Project Preparation Facility (€ 2 million), Consensus III (€ 2 million).

In addition, for the first time, Slovenia participated in the opening of the Fifth Research and Technological Development Framework Programme (€ 1.5 million) and

in the Community programmes (€ 1.25 million) of Leonardo da Vinci II, Socrates II, Youth and SME.

Implementation of the Phare Programme in Slovenia improved considerably in 1999. The programme was implemented under the Decentralised Implementation System. Implementation of the programme was affected significantly by the strengthening of the only Implementing Authority in Slovenia, the CFCU in the Ministry of Finance. The assignment of a Financial Officer to the Delegation contributed to increased efficiency in the management of Phare contracting procedures. With the support of the CFCU, the National Fund (set up in 1998) supervised financial management and eased the transfer of funds to the final beneficiaries in Slovenia.

The performance of the Phare Programme in terms of contracting and payments has substantially improved. By the end of 1999, all 1990-1997 programmes were fully contracted; € 27.5 million was contracted in 1999, almost entirely under the DIS. In the same period € 63 million was allocated to Slovenia, requiring a significant effort in 2000 to double the amount of funds contracted and to maintain a limited backlog.

Results

Phare also achieved positive results in a number of key sectors during 1999.

The **public finance sector** provides an excellent example of Phare cooperation in Slovenia. Phare has been providing support to the sector since 1993 and projects have been successfully completed in a range of different areas. In particular, Phare has carried out activities in support of the Slovene tax reform. Projects in this area contributed to the successful introduction of value added tax on 1 July 1999, by providing advice on the legislative framework, the introduction and implementation of VAT and the reorganisation of the administration; by raising general awareness about the reasons for VAT and related procedures; by implementing and testing IT specifications for VAT accounting. At the same time, the projects assisted the introduction of excise duties, in particular by defining basic functions and appropriate organisational and IT functions necessary for the collection of excise duty.

In the **energy sector**, Phare support dates back to 1993. Support has been provided for the preparation of the law on energy, which was eventually adopted by Parliament in October 1999 and which will lead to the opening up of the energy market in the electricity and natural gas sectors. Support from Phare is also being provided through the 1999 programme for the independent regulatory body. Phare has also contributed to the development of the Energy Conservation Strategy through the provision of equipment to encourage the use of renewable energy sources, like solar energy and biomass.

In the **environmental sector**, major investments have been undertaken in infrastructure (waste water treatment plants and sewage systems) under the Cross-Border Cooperation Programmes throughout the entire period of the 1995-1999 Multi-Annual Programme. In particular, the aim of the ECO-ADRIA project is to increase waste water treatment capacity in the Slovene region bordering Italy, in order to reduce the level of pollution of rivers flowing from Slovenia to Italy and to the Gulf

of Trieste; € 6.5 million was allocated to this project. In 1999, the Phare project in the Municipality of Vipava was completed; a sewage collector, a pumping station and a discharger to tie the municipal waste water system into the new treatment plant were built while other villages in the Vipava area (which had no sewage treatment capacity and were therefore discharging directly into the river) have been linked to the Vipava treatment plant.

Case study: Activating local potential in depressed areas

The aim of this project was to define cost-effective active employment measures on a regional basis. Three partnership agreements were developed in the regions of Posavje, Koziansko and Ptuj as tools for the concrete support of local employment initiative projects.

The project lasted 17 months and was divided into 3 components

- support for the local employment initiatives projects
- assistance in the establishment of an effective financial structure
- assistance in the elaboration of a national strategy.

The project achieved remarkable results, including

- the development and implementation of five integrated development plans for five regions: Ptuj, Posavje, Kurosaki, Dravina Valley and Celje
- the establishment in Celje of a fully equipped information research resources centre with fully trained staff
- the provision of a financial accounting and control system for the partnerships
- the training of 388 people, as well as 85 workshops undertaken, 4 partnership coordinators and 4 researchers trained, 12 people trained in fund-raising and lobbying issues and fellowship training for 35 people.

All these actions have long-term effects. Seventy different projects have been facilitated in the three regions and a total of six partnership programmes had been established by the end of the project in the three regions. All partners have benefited from the project in terms of improving the share/flow of information, a better understanding of the programmes of the different partners, a better coordination of existing activities, the development of a shared vision of future activities and the joint development of cooperative initiatives and projects.

The project's total cost was € 449,740.

Non-candidate countries

Albania

The year in review

Albania has faced a difficult and turbulent context time the last few years. In 1999, the country was hard hit by the Kosovo crisis. Albania witnessed the influx of over 460.000 refugees at the height of the crisis. This would have imposed a considerable burden on any country –but especially for a small and fragile country like Albania struggling to establish political and economic reform. The Albanians' response to the crisis won widespread admiration.

The launch by the EU of the Stabilisation and Association Process for five countries of the region in May 1999 gave an encouraging political sign to Albania and opened new perspectives for the country in terms of long term integration into EU structures.

The Albanian authorities managed to maintain macroeconomic stability despite the severe challenges resulting from the Kosovo crisis. GDP is estimated to have grown by 8 percent in 1999, inflation is close to zero, and external reserves are at a comfortable level.

Kosovo crisis

In June 1998, Albania had to face a first refugee crisis, for which the European Commission allocated € 1,5 million. The start of NATO air strikes, on 24 April 1999, caused a major influx of refugees from Kosovo to Albania which had to host more than 466,000 people at the height of the crisis. ECHO, the European Community Humanitarian Office, provided a swift response in the form of food, shelter, health care, water and logistics to face the emergency situation.

Macro-economic assistance

The EU provides macroeconomic assistance to Albania in the form of balance of payment support to help the IMF-designed stabilisation and adjustment programme. From 1991 to 1999, the EU has provided € 20 million in balance of payment support. In 1999, specific budgetary support (€ 60 million) was granted to Albania to support additional expenditure for hosting Kosovo refugees.

Despite the repercussions of the temporary massive influx of Kosovo refugees (these repercussions were to a large degree offset by the substantial humanitarian aid provided through the EC Humanitarian Office (ECHO) in favour of refugees, host families and health and social institutions), the authorities have shown continuing commitment to macroeconomic stabilisation policies and economic reforms. With continued financial support provided by the international community (an emergency donor meeting, organised jointly by the European Commission and the World Bank (Brussels, 26 May 1999) successfully pledged US\$ 200 million to cover external

financial needs for 1999 (of which US\$ 160 million was allocated for alleviating the impact of the Kosovo refugee crisis), GDP growth is expected to continue at 8 per cent. Despite the improvement in revenue collection, owing to the application of a 20 per cent VAT rate and improved customs duties collection, achieved with the support of EU assistance (see case story), tax revenues (estimated at some 13.5 per cent of GDP in 1999) remain short of the level necessary for a sustainable fiscal position, in particular because of the low level of income tax. With the lowest level of development in Europe (GDP per capita at about US\$ 830), Albania continues to be predominantly a rural economy with 54 per cent of GDP generated by agriculture, 21 per cent by services, 13 per cent by construction and 12 per cent by industry).

Structural reforms have also been progressing and are generally on track with the IMF programme. The process of winding up the pyramid schemes is nearing its end. The privatisation of the three remaining State banks progressed properly. Important progress has also been made in small and medium-sized enterprise privatisation: as of end-June 1999, 318 out of the remaining 469 SMEs had been sold, leased or liquidated. On the other hand, progress in restructuring/privatising of large-scale enterprises in strategic sectors has been disappointing and the Kosovo crisis even emphasised the problem. In the area of customs administration reform, some important steps have been made (implementation of the revised customs code, recruitment of new anti-smuggling officers, adjustment of reference prices for imports in line with market prices). However, the capacity of the judiciary to implement new legislation in an efficient way, in particular to repress fraud and corruption, needs to be reinforced.

Albania's overall level of development remains very low. In particular, institutions at all levels of the State, the legal framework and law enforcement are not yet adequate to lay solid foundations for a more stable democratic society and a viable and sustainable economy. Durable progress in stabilising essential State institutions remains fragile. The periodic recurrence of social disorder and rising crime, at a point where institution building is still in its inception phase, could undermine the progress achieved so far. Also, in the economic area, Albania faces a number of constraints and issues which will need to be addressed: a non-performing financial sector and a tendency to develop extra-legal economic activity; a dilapidated and inadequate infrastructure; the collapse of the industrial base; the virtual disappearance of Albanian products from domestic markets; the development of high levels of unemployment.

The fragile internal and regional security situation, considerably worsened by the Kosovo crisis in the north-east part of the country, constitutes a major obstacle to the proper exploitation of the country's natural and human resources.

Phare in 1999

In 1999, a budget of € 40.9 million was allocated to Albania under the Phare programme to reinforce essential State institutions and to stimulate economic development through improved infrastructures.

In 1999, specific budgetary support worth € 60 million was granted to Albania to support additional expenditure for hosting Kosovs refugees.

In addition, € 1.6 million was committed separately to the TEMPUS inter-university cooperation programme in 1999.

The main priorities of the **1999 programme** were aimed at

- comprehensive **administrative and institutional reform**, including support for the customs administration, the police, the judiciary, the supreme audit institution and statistics
- the **effective management of Phare resources** through the establishment of a Central Financing and Contracting Unit (CFCU)
- the **development of major and essential infrastructures** (roads and water supply/sewerage)
- the stimulation of **local development initiatives**, including job creation through support for essential local infrastructures
- assistance to the **agricultural sector**, the country's main economic sector.

Despite delays in **programming and implementation** due to the disturbances of 1997 and the Kosovo crisis, overall implementation of Phare assistance remains satisfactory.

Achievements

A number of ongoing Phare programmes made good progress during 1999.

▪ **Institution building and strengthening**

Strengthening the administrative capacity of the Albanian State is essential to achieve necessary reforms and to establish the rule of law. The continued high levels of corruption in public administration and the judiciary together with organised crime have considerably undermined the efforts of the government.

Judiciary and prisons: the EU continued in 1999 to help Albania develop a modern judiciary system compatible with EU standards in the framework of a joint programme with the Council of Europe in the organisation of the judicial system; a Plan of Action includes ongoing for monitoring the reform. Legal and regulatory frameworks have been put in place, assistance has been provided to the Ministry of Justice and other judiciary institutions and training programmes have been organised in the School of Magistrates. The EU is also improving the physical infrastructure of court facilities and is providing support for the rehabilitation of the prison system, in order to improve its quality and standards for inmates.

Police development: (see case story below).

Public sector reform: the main aim of the assistance which the EU is providing to public sector reforms in Albania is to establish efficient self-sustaining public administrations compatible with those in the EU. Together with the OECD, the EU implemented the SIGMA programme in 1999 to enhance the professionalism of the civil service.

Customs administration: (see case story below).

Statistics: the last census organised in Albania dates back to 1989. Since then a considerable internal and external relocation of the population has occurred and socio-economic patterns have undergone major changes. The present government lacks a clear picture of the current geographical distribution of the population and its composition. These figures are essential to design policies and to achieve adequate budget allocations for local communities. The EU, together with Italy, Greece, Switzerland and the Council of Europe, is providing assistance to INSTAT, the national statistical institution, for organising a population census in the year 2001. Support is foreseen at all stages of the census: preliminary organisation, management of field operations, data processing and analysis.

- **Development of infrastructures**

Improving the basic infrastructures of energy, transport and water networks are crucial for facilitating economic growth in Albania. Public services and infrastructures are generally scarce and of low quality. Ensuring improved access to many villages and remote urban districts is critical to raise standards of living and to increase the potential of the communication network inside Albania, as well as between the region and the EU.

Transport: the EU continues to support the construction of roads along the East-West corridor (No. 8) and the North-South axis. The European Investment Bank (EIB) has been a key partner in these road development projects. The EU is helping to prepare designs for a new link road to the Rinas airport, the only international airport in Albania and along the East-West corridor and the North-South axis. A Transport Master Plan, encompassing road, rail, civil aviation and maritime networks is being designed with the help of EU specialists to prepare the future investment strategy in this key sector.

Water: the water sector is considered as a key area for infrastructure development in Albania. Water supply and distribution networks continue to deteriorate. The inadequacy of sewage networks and absence of wastewater treatment are a cause of major concern. The government has developed a clear strategy for improving water supply, which requires significant financial support from donors. The EU's programme implementation unit plays a key role in stimulating and coordinating donor intervention in the water sector, as well as in implementing construction and rehabilitation works.

- **Local community development**

Through its local community development programme, the EU provided funding for hundreds of projects at local community level in Albania in 1999. Most projects, identified on a demand-driven approach, aim to build or repair public infrastructures to be operated by the beneficiary local governments. The main objective is to improve access to remote areas, improve public services such as water, primary education and health and to achieve higher standards of living by improving the urban environment. The projects include training in regional planning for local government staff.

▪ **Agriculture**

The agricultural sector has undergone a radical reform process in the past years, focused on land distribution and market liberalisation. Much progress has been achieved in this sector, but major challenges remain, such as the enforcement of the new legal framework and the development of market and service infrastructures to meet the new needs of farmers. The EU is providing technical assistance to face these challenges and provided policy advisory services to the Ministry of Agriculture in 1999.

▪ **Cross-border cooperation**

The EU cross-border cooperation programme continued throughout 1999. It is of particular importance to the Albanian government as it offers a further opportunity to open up the country and develop closer links with its immediate EU neighbours, Greece and Italy. The Albanian-Greek border region is isolated, rural and mountainous. The main economic activity is agriculture and the region suffers from labour market problems and unemployment, resulting in a high level of emigration to Greece. The cross-border cooperation programme aims to overcome the socio-economic gap between bordering Albanian and Greek regions. The purpose of the Albanian-Italian cross-border cooperation is to focus on regions of Albania which have a common maritime border with Italy, in order to improve and expand transport infrastructure.

▪ **Education**

Reform of the technical school system in Albania is essential to adapt the skills of the labour force to the new needs of the labour market. The EU is providing assistance to the Ministry of Education and Labour to reform Albanian vocational and educational schools. At university level, Albania takes an active part in the EU inter-university exchange programme, TEMPUS. Albanian universities are collaborating with their EU counterparts in joint projects and individual mobility grants are being provided for students and professors.

▪ **Democracy and human rights**

The EU is providing assistance to NGOs working in the field of democracy and human rights under its European Initiative for Democracy and Human Rights. Projects include raising awareness on the role of human rights in building a civil society, the production of radio and TV programmes promoting understanding and tolerance and support for journalist networks, etc.

Case Studies: Customs and Police

Collecting essential revenues for the State: customs

Customs duties form an essential part of Albania's public revenue. Following the civil unrest in 1997, the customs service lost control of the ports and border crossings, and consequently of its potential for revenue collection. At the request of the Albanian government, the European Commission deployed a Customs Assistance Mission in Albania (the CAM-A programme), in June 1997, to help restore control and at the same time develop a viable modern customs service. The primary objectives were to help the Albanian customs service restore control over border crossings, regulate customs revenue collection and combat smuggling and widespread corruption.

CAM-A continued throughout 1999 and included the creation of a Pre-Arrival Intelligence System (PAIS), a sophisticated computerised device to track carriers en route from neighbouring states. Customs legislation and implementation have been brought into line with European and WTO standards. For customs enforcement, an anti-smuggling service with 24 teams has been recruited, trained and deployed. The central structure of the intelligence service with headquarters and regional services has been created, including the recruitment and training of special officers.

Today, Albania is the leading country in the region in terms of anti-smuggling capacity and intelligence development.

Training Police Officers

The police force has a major role to play in civil protection and law enforcement. Albania's massive civil unrest in 1997 clearly demonstrated the need to reinforce the police's operational capacity. The EU assisted in the establishment of the multinational advisory police element (MAPE) managed by the Western European Union (WEU), to provide advice and training to the Albanian police.

Twenty-three WEU officers work on a day-to-day basis with their Albanian counterparts. The EU provided new uniforms, police vehicles, spare parts and protection devices in 1999. Police training centres (such as those in Tirana and Durres) are being renovated and equipped, to host intensive training sessions of 8 to 9 weeks. By the end of the year 2000, the EU will have trained 1,300 Albanian police officers.

To enable the police to make the best use of modern technologies, an Information Technology Master Plan is to be developed. The EU is also assisting the Albanian authorities in preparing a strategy for the medium-term development of the Albanian police. This includes drafting legislation on professional police regulations as well as on policing economic crime.

Bosnia and Herzegovina (BiH)

The year in review

1999 marked the end of the large-scale, post-war reconstruction period in Bosnia and Herzegovina (BiH); post-war BiH is made up of two Entities: the Federation of Bosnia and Herzegovina and Republika Srpska. BiH has been one of the most highly assisted countries in the world. Major internationally financed reconstruction has taken place in the infrastructure sector and has encouraged economic growth. As this assistance will decline significantly over the coming years, the economy of BiH must face the challenge of realising self-sustaining growth.

Following progress in the immediate post-war period (1996-97) in establishing the essential institutions of the country and in rebuilding the basic infrastructure of the economy, the authorities embarked in May 1998 on an ambitious economic reform programme, supported by the IMF stand-by arrangement. Under this programme, the authorities have managed to reduce macroeconomic imbalances, and the credibility of the currency board arrangement and acceptance of the Convertible Marka (KM) have increased considerably. The programme has succeeded in reducing country-wide inflation to single digits and economic reform has progressed.

However, a difficult political environment, governance problems, and the fallout from the recent conflict in Kosovo have undermined performance. Real GDP growth in 1998-99 fell short of expectations and the pace of structural reform has been disappointing in many respects. After a promising start, progress in developing BiH's basic economic institutions has been slow, and, despite the substantial contribution of the international community, and the EU in particular, to the reconstruction effort, the country's infrastructure remains weak. Territorial divisions along ethnic lines continue to hamper integrated policy implementation, particularly economic reforms. Fundamental reforms that were delayed include the privatisation of banks and enterprises and the harmonisation of excise taxes across Entities; on 8 June 1999, the Entities agreed on a list of harmonised excise taxes but it took more than 9 months to fully implement the agreement.

Progress in some other structural reforms has been better, with the most impressive strides made in the operationalisation of State institutions. The pace of structural reform increased in 1999 with the implementation of several key measures. By far the most successful achievements have been the consolidation of the Central Bank and the introduction of the new currency. In this regard, the rapid acceptance of the KM throughout the country is a testament to the sound implementation of the currency board. Important progress in inter-Entity cooperation was also made with an agreement on a common, country-wide customs tariff regime in mid-1998. In parallel, barriers to the internal movement of goods and people have also been eliminated. In 1999, the authorities also took steps to eliminate most sales tax and customs exemptions, reform the payments system and initiate the process of BiH's accession to the World Trade Organisation.

Although macroeconomic policy implementation in 1998-99 suffered some setbacks and macroeconomic developments in 1999 were affected by Kosovo, progress in this

area has been on the whole positive. The maintenance of fiscal discipline has been a key factor in this respect, and, in retrospect, BiH appears to have weathered the Kosovo conflict quite well. Since mid-1999, there have been promising signs of recovery in production and trade - especially in the Federation - and real GDP growth was estimated at 10 percent in 1999, following growth of 15 percent in 1998. Inflation, meanwhile, has continued to decline.

After four years of intensive reconstruction supported by unprecedented external aid, BiH still faces immense challenges to achieving sustainable development. Unemployment remains at about 40 per cent of the labour force. Structural deficiencies affect most areas of the economy and discretionary administrative intervention in the economy encourages corrupt practices, limits the development of the private sector and inhibits foreign direct investment.

BiH is now at a crossroads. In terms of external funding to fuel investment and economic growth, sources are beginning to dry up. The main challenge facing the authorities now is to press ahead with structural reforms in order to establish conditions conducive to the development of the private sector and to lay the basis for fiscal sustainability.

Through the launch of the Stability Pact and the Stabilisation and Association Process in 1999, the EU has opened new perspectives for BiH in terms of future possible integration into EU structures. Future assistance to the country will be linked to this process.

Phare and Obnova in 1999

In 1999, the Phare and Obnova programmes were the main instruments for EU assistance to BiH, both in a complementary way. Obnova mainly focused on the **reconstruction process and the return of refugees**, while Phare assistance focused on projects in **direct support of the peace agreements**, in particular the building of **cross-entity links** (BiH is not eligible for full Phare assistance). The European Community Humanitarian Office (ECHO) is now in the process of phasing out its operations in BiH due to the improvement of the overall humanitarian situation.

The total allocation (Phare and Obnova) for BiH in 1999 was € 118 million. More than half of this budget was allocated to **reconstruction projects to facilitate the return of refugees and displaced persons**. Other priorities aimed at laying the groundwork for

- **sustainable economic development**
- **democratisation**
- **institution building**
- **civil society and social development.**

Apart from Phare and Obnova, BiH also continued to benefit from **humanitarian assistance** (ECHO) with € 58.9 million in 1999.

Macroeconomic assistance was given to the country in 1999 in the form of balance of payments support worth € 60 million.

Achievements

▪ Reconstruction of infrastructures

During 1999, major country-wide reconstruction projects funded by the EU were completed. Water and electricity networks were repaired, bridges rebuilt, kilometres of roads rehabilitated, hospitals rebuilt and equipped, minefields cleared, schools, kindergartens and universities re-opened and telephone lines restored, etc. The airports of Sarajevo, Mostar and Banja Luka were repaired and upgraded. Due to the extensive damage inflicted to Mostar and Sarajevo, these two cities have benefitted from various integrated reconstruction programmes, which became highly visible in 1999.

▪ Return of refugees and displaced persons

As part of its major effort to help refugees and displaced persons to return to their homes of origin, the EU has to date rebuilt more than 40,000 houses all over the country, with a clear emphasis on regions where returns are most likely to happen. But repairing roofs is not enough to encourage people to come back: they need jobs, schools for their children, healthcare, social security, etc. That is why the reconstruction of houses must go hand in hand with the rebuilding of health centres and schools and the revival of small businesses. The EU's principal partners in this type of integrated return projects are NGOs.

But there are not enough reconstruction grants for all the affected BiH families. This is why the EU has set up a housing finance programme in collaboration with local commercial banks. Individuals can gain access to loans to rebuild their houses through this programme which has a double objective: to improve housing supply and at the same time establish a sustainable financing system for housing construction in BiH. In 1999, the nine partner banks participating in this housing loan project approved 1,650 loans totalling € 14.25 million.

One of the pivotal problems hanging over the refugee and displaced persons return process in BiH involves property rights. The EU continued to fund a substantial part of the Commission for Real Property Claims in 1999, which is an institution created by Dayton to help people regain the property they lost during the war.

▪ Democratisation and reform

Support for democracy and human rights in BiH is essential for continued stability and the country's future integration into Europe. In addition to the support that the EU continued to give in 1999 to the two bodies of the Commission on Human Rights, set up to pursue the fundamental rights and freedoms of the individual, the EU is also providing funding for projects which assist the strengthening of a democratic society. Funded projects include those that promote the rule of law, respect for human rights, protection of minorities and political pluralism (including support for an independent media).

The EU is also actively participating in the reform of the health and education system in BiH. The successful Vocational Educational Training (VET) programme, set up to reform technical schools through partnerships with technical schools from the EU, ended at the beginning of 2000. At university level, the European Commission is running the TEMPUS inter-university cooperation programme in BiH.

The EU health reform programme includes institutional support, health financing, assistance to the pharmaceutical sector and primary health care development. The reform programme aims to build a sustainable health sector in BiH which until now has been heavily dependent on humanitarian assistance. Several projects in this field were implemented during 1999, including one to rebuild and re-equip the Laboratory for Quality Control of Drugs.

- **Institution building**

The EU is supporting the new State of BiH in drafting new laws, in particular in the fields of foreign trade and investment and commercial legislation. EU lawyers continued to collaborate throughout 1999 with their BiH counterparts within the EU/BiH Consultative Task Force (CTF), with the aim of setting up a legal system compatible with that of the EU.

Assistance to the common State institutions is essential to the success of BiH's existence as a single state. So far the common institutions have worked very weakly compared to the administrations in the two Entities (Federation of BiH and Republika Srpska). EU experts are laying the groundwork to set up a professional civil service in the common institutions: the Presidency, the Parliamentary Assembly and the three line Ministries. Assistance is also being given to the Constitutional Court and the Central Bank. Support to Police Academies and assistance to judicial reform were part of the EU's institution strengthening programme in BiH in 1999.

BiH is for the first time a single and uniform customs territory: this is the tangible result of the highly successful Customs and Fiscal Assistance Office (CAFAO) programme funded by the EU. The CAFAO programme, which includes assistance from approximately 30 European customs and tax experts, is contributing to the development of customs and tax systems in BiH based on modern European standards (see case story)

- **Economic regeneration**

The EU has helped put on track the Central Bank of BiH by training its personnel and by assisting the launch of the new currency: the convertible Mark. It is also trying to promote business in BiH by streamlining legislation to make it more user friendly for businessmen. The EU has started supporting the Foreign Investment Promotion Agency (FIPA) which will promote BiH as a location for investment.

The EU-funded Industrial Development Programme for BiH provided technical assistance to the Wood and Furniture sector in 1999, one of the most promising sectors which fell apart during the war and which now has to face up the challenge of

transition to a market economy. This project has had tangible results in attracting EU partners.

Through the Micro-Enterprise Bank (MEB), the EU has helped to develop credit finance for SMEs in BiH. More than 120 loans to SMEs were disbursed in 1999.

The EU has put considerable resources into reviving the agricultural sector in BiH. Assistance to farmers has produced highly visible results. The EU has provided supplies, livestock, seed capital, equipment and planning strategies to support a modern agricultural policy for the government. Assistance in forestry management and protection was also provided by the EU in 1999.

The EU continued to run various job creation programmes all over the country in 1999 with NGOs or international organisations, including the United Nations Development Programme.

Case studies:

Customs and Fiscal Assistance Office

Since 1996, the Customs and Fiscal Assistance Office (CAFAO) programme, funded by the EU, has been assisting the State and Entity authorities of BiH to implement the customs and tax related provisions of the Dayton Peace Agreement. In late 1997, the CAFAO programme was expanded to include taxation.

The CAFAO programme, which includes assistance from approximately 30 European customs and tax experts, is contributing to the development of customs and tax systems in BiH based on modern European standards. It includes management, legal, structural, procedural, computer, training and investigation support components.

In terms of customs, the key items of customs policy and tariff laws are now all in place, and BiH has a single and uniform customs territory for the first time. The administration of customs and customs procedures is an Entity level responsibility and the CAFAO programme is therefore working with the Federation and Republika Srpska to draft identical Entity-level implementing legislation and regulations to reflect the State Customs Law. This is being simultaneously supported by the delivery of specialist training on each customs regulation to local customs officers. Such training follows general training delivered to all customs officers by the CAFAO programme.

The CAFAO programme is also focusing on assisting the Customs Services to enforce the law. A significant step forward in fighting customs crime was the creation during 1999 of Customs Enforcement sections within each Entity Customs Service. The CAFAO programme provided the Sections with both classroom and on-the-job training, as well as all equipment necessary to enforce the Customs Law. The Sections will be further consolidated with the future introduction of Customs Enforcement legislation, including provisions on penalties, powers and offences. The Customs Enforcement Sections' activities are also being supported by the CAFAO-initiated

“Customs Hotline” established in each Entity in September 1999. This ongoing advertising campaign is encouraging the people of BiH to assist in the fight against customs crime by reporting via a dedicated telephone line any information they believe could assist the Customs Services.

Action is also being taken to ensure that customs staff themselves uphold and enforce the law and prevent possible internal corruption, with the CAFAO programme assisting the authorities to introduce internal audit and management assurance functions.

The introduction of a countrywide customs computer system (ASYCUDA++) is the final and essential element in the modernisation and development of customs in BiH. Joint Entity project groups, supported by CAFAO, are currently developing a prototype of this computer system for future pilot testing, to be followed ultimately by full implementation in BiH. The system will handle all data associated with the clearance and movement of customs goods within BiH and will also assist the authorities to selectively investigate suspected cases of customs crime.

Taxation

The CAFAO programme is also providing assistance in the taxation field, although this is essentially confined to the establishment of effective control and enforcement structures in each Entity Tax authority. This includes the possible establishment of centralised headquarters-level specialist units to control larger traders throughout each Entity and centralised headquarters-level tax investigation units to investigate cross-Cantonal, cross-Entity or internationally linked tax fraud. The CAFAO programme is also encouraging the introduction of the more structured collection of identified tax liabilities, which to-date has not been properly addressed by local authorities. These initiatives are intended to support the introduction of modern and efficient tax authorities, aimed at maximising revenue collection and the generation of public revenue for BiH.

So far the EU has allocated € 41 million to CAFAO activities.

The Former Yugoslav Republic of Macedonia (FYROM)

The year in review

During the first quarter of 1999, the new government, which took office in December 1998, adopted an ambitious programme to boost the economy, reform legislation and the public administration, reduce unemployment, increase foreign direct investment and improve inter-ethnic relations, as well as relations with neighbouring countries. A central feature of the government's policy is the country's integration into Euro-Atlantic structures.

A cooperation agreement and an agreement in the field of transport with the European Community have been in force since January 1998. Two cooperation councils have been held between the European Community and the Former Yugoslav Republic of Macedonia (FYROM). The last cooperation council stressed the positive record of the country in terms of political and economic reforms, as well as the improvement in inter-ethnic relations; the significant role of the country and, in particular, its contribution to regional stability, security and cooperation was underlined.

1999: stabilisation and association process

On 26 May 1999, the European Commission proposed the creation of a stabilisation and association process (SAP) for Albania, Bosnia and Herzegovina, Croatia and FYROM. The SAP provides a new framework for the development of relations between these countries and the EU. It includes the possibility of concluding a stabilisation and association agreement, a new kind of contractual relationship with the EU. The stabilisation and association process represents a historic turning point in the relations of the EU with the countries of the region - for the first time, it offers a prospect of EU integration.

FYROM is the first country of the region to have started negotiations with the EU for the conclusion of a stabilisation and association agreement.

On 16 June 1999, the European Commission adopted a Report on the Feasibility of Negotiating a Stabilisation and Association Agreement with FYROM.⁴ The Commission assessment concluded that, taking into account the political and economic reforms undertaken, notably in the framework of the Co-operation Agreement and relevant Community assistance, and after reasonable transition periods, depending on the areas concerned, FYROM could be in line with the requirements of a Stabilisation and Association Agreement. On this basis, the Commission report considered it feasible to envisage the opening of negotiations for such an agreement.

⁴ Com (99) 300 of 16.6.99

The government has a very ambitious legislative programme. However, despite its size, the capability of the public administration to implement and enforce legislation is weak. This is particularly so at local level. Policy making skills within the public administration are generally low and in need of development. While judges are appointed by an independent agency, the Republican Judicial Council, and confirmed by Parliament, the judicial system is overloaded and slow. It is widely recognised by both the government and international donors that public administration reform, including the reform of the court system, is fundamental for the successful transformation of the country, which is essential to bring it closer to the EU. A number of donors, including Phare, are actively supporting the government in its efforts to reform the administration.

The government coalition, which is composed of four parties and enjoys a substantial Parliamentary majority, has displayed a determination to address issues causing inter-ethnic tensions in a number of areas. A major step was taken with the adoption of the Amnesty Law that led to the release of the mayors and presidents of the municipal councils of Tetovo and Gostivar, who were imprisoned after the events of 1997. An increase in ethnic Albanians in the public administration has been noticeable under the new Government.

The Government has given priority to strengthening the country's relations with its neighbours and to resolving sources of disagreement. The longstanding impasse in relations with Bulgaria has been resolved and a number of co-operation agreements between the two countries have been signed. Three co-operation agreements have been signed with Albania in the sectors of agriculture, employment and social security, as well as two protocols for co-operation in the fields of foreign policy and defence.

Economic performance

Following the successful stabilisation of the economy in 1995, largely linked to the decision to peg the local currency to the Deutsche Mark, growth resumed in 1996. However, low levels of investment, including foreign direct investment, and insufficient progress in structural reforms in the enterprise and financial sectors resulted in a fragile balance of payments situation.

In July 1997, the denar was devalued by 14 per cent in consultation with the IMF. This was accompanied by a programme of adjustment providing a tightening of fiscal policy and a step-up of efforts to address structural problems. This strategy worked well. In 1998, export growth picked up, stimulating industrial production. Real GDP growth increased to 2.9 per cent, helping to reduce the large level of unemployment to 34.5 per cent of the labour force, from 36 per cent in 1997. At the same time, the authorities maintained their tight fiscal and monetary policies, in support of the need to increase export competitiveness, maintain the exchange rate anchor and attract more FDI. The already low inflation was eliminated.

Despite export growth surpassing import growth in 1998 for the first time, the current account deficit increased again both in dollar terms (to US\$ 290 million) and in proportion to GDP. At the beginning of 1999, the improvement in competitiveness

(notably because of moderate wage developments and very low inflation) was expected to continue and to contribute to a reduction in the current account deficit.

Structural Reforms

Upon independence, FYROM was confronted with very fragile enterprise, agricultural and financial sectors, as well as with weak - if not non-existent - institutions supporting the functioning of a market economy. Important new laws have been introduced in recent years focusing on property rights and the basic institutions of a market economy (Law on public enterprises and a new Commercial Code in 1996, Law on Bankruptcy and Law on Movable Collaterals in 1998).

Progress in the area of privatisation has been mixed. Although more than 80 per cent of companies are controlled by the private sector as a result of an ambitious privatisation programme implemented as from 1995, corporate governance has not improved sufficiently due to the methods of privatisation that have been used (essentially management and employee buy-outs). Moreover, progress has been slow in tackling the problems of core loss-making enterprises. The authorities undertook to begin preparations to sell or liquidate twelve loss-making enterprises in the second half of 1999. Important measures are also being taken to extend privatisation to previously socially-owned agricultural enterprises.

The financial sector remains fragile, although important restructuring measures have been undertaken, including in the context of IMF-supported programmes.

Impact of the Kosovo Crisis

While estimates of the economic impact of the crisis in Kosovo are fraught with uncertainty, it is clear that the crisis has had a negative impact on the economy of FYROM in a number of ways, including the influx of refugees, disruptions in trade relations and lower investment flows.

At the height of the crisis, in June 1999, some 245,000 refugees were hosted in FYROM, equivalent to about 11 per cent of the total population. In addition, some 87,000 refugees had already been evacuated from the country. Notwithstanding the political consequences on the country's delicate ethnic balance, this very large influx of refugees has had a serious impact on social conditions.

The crisis has also had a very strong impact on trade, in particular as a result of the closure of the main transit Route through the Federal Republic of Yugoslavia (FRY). FYROM's exports to FRY and other trading partners have been seriously disrupted. In 1998, the FRY was the second most important trade partner, immediately behind Germany. Trade flows with the FRY represented 18.2 per cent of FYROM's exports (totalling US\$ 1.3 billion) and 12.6 per cent of its imports (totalling US\$ 1.7 billion). In addition, it is estimated that almost 50 per cent of total exports and 38 per cent of total imports were transiting the FRY. In the context of the Kosovo crisis, trade has been falling sharply. Contracts have been lost, both to the FRY and to other markets due to higher transit costs, increased uncertainty and a temporary shortage of critical imports.

Investment flows declined sharply, notably because of the impact of higher economic and political risks posed to potential investors and more difficult access to foreign borrowing and trade finance.

The abrupt fall in external demand, although compensated partly by a fall in imports, was likely to have a severe negative impact on real GDP growth. The IMF estimated that, even with the required external financing, GDP would have contracted by at least 8 per cent in 1999 rather than the expected 5 per cent growth.

However, the reconstruction of Kosovo which began in the second half of 1999 made it possible for the country to perform much better than foreseen, with an overall growth of 2.7%, due to the growth in trade and services.

All these elements will have an important impact on the fiscal situation. Expenditures will increase, notably those linked to the refugees (by 2.5 per cent of GDP, according to the IMF) and the social funds (by 1.5 per cent of GDP). Import duties (17 per cent of total public revenues in 1998) will fall in line with imports while negative real GDP growth will translate into lower tax revenues. Overall, the 1999 fiscal deficit is expected to increase from a planned 0.2 per cent of GDP to 4.9 per cent.

Phare and Obnova in 1999

A total of € 15 million was allocated to FYROM under the 1999 Phare budget to facilitate the process of economic and social transformation towards a market economy and to strengthen the institutional and administrative capacity of the state.

The Phare 1999 programme covers five sectors

- continuation of the **SME development programme**, with an allocation of € 6.2 million, which provides technical assistance to the National Enterprise Promotion Agency and the Regional Enterprises Support Centres (RESCs) established under the previous Phare programme, as well as funding for RESCs which became operational at the end of 1999; further funds are being provided for the micro-credit line for SMEs, which have a critical role to play in the economic recovery of the country
- support to **local government development**, with an allocation of € 2 million, to provide assistance to the newly created Ministry of Local Self-government, pilot municipalities and associations representing local government
- a programme for the **agricultural sector**, which provides assistance for policy formulation, strategy development, institution strengthening and harmonisation of legislation; the programme focuses, *inter alia*, on livestock, to help FYROM comply with international standard requirements, particularly in relation to animal identification systems and databases
- a € 3 million programme to strengthen the capacity of the newly established **Ministry of Environment**, which concentrate on the revision and preparation of legislation, environmental permitting and enforcement, training and the preparation of strategies on environmental awareness raising, communication and data management
- support to the **social sector**, with an allocation of € 2 million, to improve the management capability of the Ministry of Labour and Social Policy, so that it can better fulfil its responsibilities and to assist social welfare centres and social

institutions to adapt and modernise their standards to levels which approximate to those in the EU.

FYROM also benefits from the **Cross-border Cooperation Programme** with Greece, which is primarily focused on infrastructure projects to improve Pan-European Corridor X and modernise two key border crossings.

In addition to Phare support, assistance under the **Obnova (Reconstruction in the Former Yugoslavia) Programme** was granted in May 1999 in the form of a € 25 million budgetary support programme to ease the burden of the Kosovo crisis. A further € 80 million in macroeconomic assistance has been given to the country.

The European Community Humanitarian Office, ECHO, restarted its activities in FYROM as a consequence of the Kosovo crisis, to bring **emergency aid** to the refugees and the vulnerable among the Macedonian population.

The **implementation** of the first series of Phare projects began in the first half of 1997, with the process continuing in 1998 and 1999. Virtually all the projects from the 1998 allocation are at the tender stage. A considerable number of the projects experienced common implementation difficulties, stemming from limited absorption capacity and inexperience on the part of beneficiaries in relation to internationally funded assistance projects. The government has been making concerted efforts to address these difficulties. However, the Kosovo crisis has resulted in a slow down in progress in most projects, due to the involvement of counterparts in the government response to the crisis. With the resolution of the crisis, it is anticipated that the counterparts will be in a position to play their full part in the projects.

Achievements

▪ Support to enterprises and the financial sector

The EU is supporting FYROM in its efforts to make economic and commercial legislation compatible with that of the EU through providing technical assistance to draft new laws.

In order to help develop the SME sector in FYROM, the EU has supported the creation of a National Enterprise Promotion Agency (NEPA) which acts as a representative of the SME community at policy level. The agency aims to support enterprises in improving their management, marketing and know-how in order to create competitive, export-oriented companies. The EU has also helped establish a network of Regional Enterprise Support Centres throughout the country (see case story) in order to provide entrepreneurs with direct business support services. A micro-credit scheme has also been set up to make it easier for SMEs to obtain bank loans.

Intensive training has been provided to the banking community in order to improve capabilities in credit and risk management techniques, so that the banks can better support the development of SMEs.

- **Transport (Cross-border, EIB, Phare)**

Two key transport corridors cross the country and intersect at Skopje. They form part of the EU-wide Trans-European Networks (TENs), and are known as Corridor 8(E-65 East-West: Durres-Tirana-Skopje-Sofia-Varna) and Corridor 10 (E-75 South-East-North: Thessaloniki-Skopje-Belgrade-Zagreb-Passau or Munich). Improvements to these roads are being funded as part of an overall programme for upgrading transport infrastructure. The EU is providing support through different sources: grants from the national programme for FYROM and the cross-border co-operation programme with Greece, together with loans through the European Investment Bank (EIB).

- **Agriculture**

The EU is assisting the Ministry of Agriculture in policy and strategy development for the transition to a market economy and in raising animal and plant health controls to EU standards. European experts have also helped to draft a new law on agricultural land, which is now in force.

- **Environment**

The EU is helping the relevant Ministries with the development of national strategies for waste water and solid waste. Support is being given to the Ministry of Environment to manage and enforce national environmental policy.

- **Education**

FYROM is taking an active part in the EU inter-university exchange programme, TEMPUS. Joint European projects are being implemented with EU universities and individual mobility grants for students and professors are currently underway.

Advice and assistance are being given to the Ministry of Education, to establish a school curriculum which is better adapted to the needs of the labour market (Vocational Education and Training - VET).

- **Social sector**

The EU is assisting the Minister of Labour and Social Policy in improving its management capabilities and social welfare institutions to adapt and modernise their standards so they are similar to those in the EU.

- **Local government development**

The main objective of the EU assistance programme for local government is to strengthen the capacity of the Ministry of Local Self-government to manage the process of decentralisation and to enhance dialogue between the different levels of central and local government.

- **Cultural development**

The EU is assisting the Ministry of Culture with a programme, which aims to develop the commercial and autonomous management of cultural institutions and provide financial assistance to upgrade major national cultural institutions, fund small projects related to cultural activities and contribute to the conservation of monuments and sites.

- **Democracy and civil society**

The EU is helping to strengthen Macedonian civil society and the social network, through funding for projects which aim to develop the activities of NGOs, for example projects to support families with disabled children or to help the social integration of marginalised Roma communities.

Support is also being given to develop an independent media, which will play an essential role in democratisation. A comprehensive audience research survey funded by the EU is currently underway in order to achieve better understanding of the overcrowded media scene in FYROM and to help develop a sound media market with self-sustainable magazines, newspapers, radios and televisions.

- **Public administration reform**

The EU is providing key assistance for the reform of the public administration. The programme which began in 1998 focuses on the civil service system, public finances, local government, courts and judicial administration. This programme will be followed by a programme focusing on local government development.

- **Statistics**

EU assistance to this sector has continued, with the aim of aligning the national statistical system to that of the EU.

Case study: Regional Enterprise Promotion Centres up and running

Five Regional Enterprise Promotion Centres (RESCs), which are a major component of the Phare Integrated SME programme in FYROM, have been opened. RESCs are new business support agencies which have been established by local founders drawn from the public and private sectors, with financial and technical assistance from the EU. Their aim is to provide a comprehensive range of information, advisory and other services for existing SMEs and for people seeking to go into business for the first time. The Centres are located in Kumanovo, Skopje, Bitola, Strumica and Veles. The five centres were all established in 1999. The RESCs offer concrete assistance in the following fields

- the preparation of business plans
- advice on credit lines, including applications under the micro-credit line provided under the Phare Integrated SME programme
- information on suppliers of equipment, sources of raw materials and the identification of potential foreign partners and export customers
- seminars and training courses
- information on international low-cost consultancy for SMEs.

RESCs are a vital part of the support which the EU is providing to develop a strong, diversified and efficient SME sector in FYROM.

Statistical overview

Phare funding by country, 1990-1999

Total Phare commitments, contracts and payments, 1990-1999, in million EUR

Partner country	Commitments	Contracts	Payments
Albania	587.13	483.42	347.71
Bosnia & Herzegovina	285.33	241.65	199.72
Bulgaria	853.83	632.41	512.94
Czech Republic	475.90	355.82	252.86
Estonia	189.70	154.85	116.44
FYROM	189.01	132.74	110.29
Hungary	967.40	695.26	598.93
Latvia	248.70	186.04	141.07
Lithuania	335.23	225.98	182.45
Poland	2,020.82	1,557.76	1,377.81
Romania	1,184.34	828.94	658.54
Slovakia	355.72	210.87	155.26
Slovenia	192.43	123.12	93.24
Czechoslovakia	232.08	232.20	228.88
East Germany	34.49	28.86	28.61
Yugoslavia	43.68	43.68	43.68
Multi-country programmes	2,033.34	1,781.57	1,306.70
Total	10,229.19	7,915.16	6,355.13

Phare funding by sector, 1990-1999

Total Phare commitments, contracts and payments, 1990-1999, in million EUR

Sector	Commitments	Contracts	Payments
Administration & public institutions	1,008.64	574.20	362.40
Agriculture	622.40	491.36	460.28
Approximation of legislation	118.33	92.33	66.73
Civil society and democratisation	152.79	92.30	76.17
Consumer protection	12.63	12.63	10.06
Education, training and research	1,067.19	1,027.95	370.26
Environment and nuclear safety	954.22	603.90	498.08
Financial sector	276.94	264.97	253.71
Humanitarian, food and critical aid	573.43	588.37	535.63
Infrastructure (energy, transport and telecoms)	2,450.88	1,765.38	1,218.58
Integrated regional measures	347.22	197.77	115.17
Other (multidisciplinary, general TA, etc.)	843.83	771.53	608.45
Private sector, privat. & restructuring, SMEs	1,266.72	1,078.62	867.82
Public health	104.08	102.35	93.09
Social development and employment	429.89	251.48	218.69
Total	10,229.19	7,915.16	6,355.13