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SERBIA 2010 PROGRESS REPORT

Accompanying the

COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

Enlargement Strategy and Main Challenges 2010-2011

1. INTRODUCTION

1.1. Preface

Since March 2002, the Commission has reported regularly to the Council and Parliament on progress made by the countries of the Western Balkans region.

This progress report largely follows the same structure as in previous years. The report:

- Briefly describes the relations between Serbia and the Union;
- analyses the situation in Serbia in terms of the political criteria for membership;
- analyses the situation in Serbia on the basis of the economic criteria for membership;
- reviews Serbia's capacity to implement European standards, that is, to gradually approximate its legislation and policies with those of the *acquis*, in line with the Stabilisation and Association Agreement and the European Partnership priorities.

The period covered by this report is from mid-September 2009 to early October 2010. Progress is measured on the basis of decisions taken, legislation adopted and measures implemented. As a rule, legislation or measures that are under preparation or are awaiting parliamentary approval have not been taken into account. This approach ensures equal treatment across all reports and permits an objective assessment.

The report is based on information gathered and analysed by the Commission. In addition, many sources have been used, including contributions from the government of Serbia, the EU Member States, European Parliament reports¹ and information from various international and non-governmental organisations.

The Commission draws detailed conclusions regarding Serbia in its separate communication on enlargement² based on the technical analysis contained in this report.

¹ The reporter for Serbia is Mr Jelko Kacin.

² Enlargement Strategy and Main Challenges 2010-2011 (COM(2010) 660 of 9.11.2010).

1.2. Context

Serbia is a potential candidate for EU membership. On 29 April 2008, Serbia signed a Stabilisation and Association Agreement (SAA) and an Interim Agreement on trade-related measures with the EU. The Interim Agreement entered into force on 1 February 2010. On 14 June 2010, the Council agreed to launch the ratification process for the SAA.

On 22 December 2009, the Serbian President and Prime Minister handed over the country's application for EU membership. The accompanying Government Memorandum highlighted that the application reflected an overall social consensus on the European orientation of Serbia and its aspiration to EU membership.

1.3. Relations between the EU and Serbia

Serbia is participating in the Stabilisation and Association Process. The Stabilisation and Association Agreement (SAA) provides a framework of mutual commitments on a wide range of political, trade and economic issues. The SAA was signed, along with the Interim Agreement, in April 2008. EU ministers agreed to submit the SAA to their parliaments for ratification and the EU agreed to implement the Interim Agreement on trade and trade-related matters as soon as the Council decided that Serbia was fully cooperating with the International Criminal Tribunal for the former Yugoslavia (ICTY). Serbia started on 1 January 2009 to implement the Interim Agreement. Following ICTY Prosecutor Brammertz's report to the UNSC in December, the Council decided to start implementing the Interim Agreement. The Interim Agreement entered into force on 1 February 2010. At the 14 June 2010 Foreign Affairs Council, Ministers agreed to submit the Stabilisation and Association Agreement to their parliaments for ratification and took note that Serbia had applied for EU membership on 22 December 2009.

The EU is providing guidance to the Serbian authorities on reform priorities as part of the European Partnership. The Serbian government has continued to implement a national programme for integration into the EU and has used quarterly reporting as a monitoring mechanism. Progress made on reform priorities as part of the European integration process is encouraged and monitored by the Interim Committee and its structure of sub-committees and the Enhanced Permanent Dialogue (EPD). An EPD plenary meeting was held in July 2010. Several sub-EPD meetings took place during the reporting period, covering all sectors of the SAA that are not included in the Interim Agreement, such as energy, the environment, social policy, justice, freedom and security. A political dialogue at ministerial level took place in Brussels in January 2010. Economic dialogue took place in a bilateral meeting with the Commission and Serbian senior officials in November 2009. Moreover, the multilateral economic dialogue between the Commission, EU Member States and potential candidate countries in the context of the pre-accession fiscal surveillance took place in an expert meeting in June 2010.

The first meeting of the Interim Committee took place in March 2010 in Belgrade. Subsequently, a number of sub-committees also met, including on the internal market, competition, transit traffic, trade, customs, taxation, agriculture and fisheries. Serbia has continued to build a positive track record in implementing the Interim Agreement.

Visa liberalisation for Serbian citizens travelling to the Schengen area was granted by the Council, after consultation with the European Parliament, as of 19 December

2009. It applies to holders of biometric passports travelling to the Schengen area. This decision was based on substantial progress in the areas of justice, freedom and security and fulfilment of the specific conditions set out in the roadmap for visa liberalisation.

As a potential candidate for EU membership, Serbia aligned itself with 51 CFSP declarations out of a total of 74 relevant declarations adopted by the EU during the reporting period (69%).

Serbia receives pre-accession financial assistance under the Instrument for Pre-accession Assistance (IPA). IPA is implemented by the EU Delegation in Belgrade. A decentralised implementation system (DIS) for managing aid remains a short-term objective for Serbia. Under the adopted roadmap, management units in line ministries have been established. Preparation for DIS has continued at a slow pace. However, further extensive efforts including on staff, are necessary in order to put Serbia in a position to take over responsibility for implementation of all IPA components and for future management of Structural and Cohesion Funds.

Serbia's national IPA allocation for 2010 totalled €197.9 million. Financial assistance focuses on areas such as strengthening the rule of law, human rights, education, transport and environmental protection. Serbia participates in the IPA multi-beneficiary programmes including in an IPA crisis response package developed in 2008. The package is fully operational in 2010. Serbia has continued to take part in cross-border cooperation with neighbouring countries across a range of areas such as infrastructure, environmental issues, cultural exchanges, research, job creation, security and crime prevention. The first €50 million instalment under the IPA 2009 budget support initiative was disbursed in December 2009. The purpose of the budgetary support is to ease the social and economic consequences of the current economic downturn in Serbia, and help Serbia to pursue the pace of EU integration-related reforms. An Agreement on Macro Financial Assistance was signed in July 2010 between the EU and Serbia.

Concerning EU programmes, the EU has co-financed Serbia's participation in the Seventh Research Framework Programme, the Culture, Fiscals 2013, Customs 2013 Programmes as well as the Programme for Employment and Social Solidarity (PROGRESS).

2. POLITICAL CRITERIA

This section examines progress made by Serbia towards meeting the Copenhagen criteria, which require stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities. It also monitors regional cooperation, good neighbourly relations with enlargement countries and Member States, and compliance with international obligations, such as cooperation with the UN International Criminal Tribunal for the former Yugoslavia (ICTY).

2.1. Democracy and the rule of law

Constitution

There has been some progress in implementing the November 2006 Constitution, which is a key priority of the European Partnership. In November 2009 the Serbian parliament adopted a Decision endorsing the draft Statute of Vojvodina, and the law determining the competencies of Vojvodina. The Statute was proclaimed in the

Provincial Assembly of Vojvodina in December 2009 and came into force in January 2010. However, as regards Vojvodina, the laws on public property and on its own resources required by the Constitution have not yet been adopted. This impedes the effective exercise of the new competencies.

Overall, implementation of the new constitutional framework is well advanced. However, the laws regulating public property and Vojvodina's own resources are still to be adopted.

Parliament

In February 2010, parliament adopted the Law on the National Assembly, required by the Constitution. The law establishes parliamentary budgetary autonomy through a separate budget as opposed to the previous practice of government-decided allocations. It also provides for procedural innovations, in particular the establishment of a parliamentary collegium which formalises the earlier *ad hoc* practice of consultations between the Speaker and the heads of political groups in the parliament. New parliamentary rules of procedure were also adopted.

The new rules of procedure consolidate the existing instruments of control over the executive and further clarify the legislative procedures. However, some provisions related to parliament's relations with other state bodies and institutions have been criticised by the Ombudsman and by the Commissioner for Free Access to Public Information as an attempt to interfere on the functioning of the independent regulatory bodies.

The current legislature has continued to be active in adopting legislation. However, the quality of the legislative output has been affected by the practice of lawmaking by urgent procedure. This continued to be used frequently and for major systemic pieces of legislation. Public consultation on content and impact of draft laws has remained insufficient.

The new rules of procedure provide for a reduction of the number of standing parliamentary committees from 30 to 19. However, this provision remains to enter into force for the next legislature. The functioning of the committees remains largely reactive and their effectiveness varies significantly. There is a lack of adequate expert and support staff to assist the committees. Parliament has continued with regular hearings of the government. However these remain formalistic rather than substantive in nature. Inflammatory and offensive language has continued, with sanctions being applied in some cases.

The electoral framework legislation has been partially revised. Parliament adopted the law on the single voter register in December 2009. This legislation regulates in a coherent and consolidated way the establishment and management of the permanent central register of voters, including Serbian citizens residing abroad. The register will take the form of an electronic database managed by the Ministry for Public Administration and Local Self- Government. However, the Law on the State Electoral Commission has not been adopted. Constitutional and legal provisions which do not meet European standards remain in force. These relate to political party control over the mandates of the MPs and parties' ability to arbitrarily appoint MPs instead of following the order of candidates from electoral lists.

Overall, further steps were taken to improve the functioning of parliament through the adoption of a new Law on the National Assembly and new rules of procedure.

However, efforts are necessary to further improve the quality of the legislative output. The electoral framework legislation needs to be brought fully into line with European standards.

Government

The government remained stable and continued to demonstrate a high degree of consensus on EU integration as a strategic priority. The government continued to implement provisions of the Interim Agreement of the SAA in line with the agreed liberalisation schedule and took additional measures in the areas of competition and state aid. The European Integration Council, chaired by the Prime Minister and involving civil society representatives, met once, giving its full political support to government European integration efforts.

The government adopted a Decision, in January 2010, activating the Coordinating Body for accession to the EU chaired by the Prime Minister. The Coordinating Body met once during the reporting period. The Serbian European Integration Office has continued to function well and was exempted from the overall cuts in numbers of employees.

The government has been drafting a number of bills aimed at further alignment of national legislation with European standards. However, the quality of the legislation was uneven and continued to be affected by inadequate impact assessment of proposed acts. The government lacks coherent rules and practices for public consultations. Effective implementation and monitoring of the adopted legislation still need to be improved.

There was no public condemnation from the government in reaction to repeated threats against the State Secretary for Human and Minority Rights for his defence of rights of vulnerable groups.

Ministries abided to a varying degree by the opinions and recommendations of independent regulatory bodies, including the State Audit Institution.

As regards local self-government, decentralisation has continued and a number of competencies have been transferred to the local level. However, this was done without ensuring sufficient capacity and resources at local level. There has been insufficient consultation with local authorities in the decision-making process relating to the development of new legislation or amendments to existing laws that have implications at the local level. The law required by the Constitution to restore public property at municipal level has not been adopted. In April 2010, the Constitutional Court ruled that the provisions of the law on local elections establishing blank resignations and allowing political parties to arbitrarily allocate seats are not in line with the Constitution.

Overall, the government continued to be stable, and the consensus on strategic priorities, including EU integration, was maintained. However, both the preparation and implementation of new legislation need to become more effective.

Public administration

There has been some progress in public administration reform.

The law on administrative disputes, which regulates judicial scrutiny of administrative acts and the work of the Administrative Court, was adopted in December 2009. As part of an arrangement with the International Monetary Fund (IMF) to reduce the fiscal deficit, a law was adopted on reducing the number of employees in the administration by 10%. The overall level of staff effectively employed in the field of European integration has been maintained. Changes to the law

on civil servants from December 2009 introduced quarterly appraisal of the work of civil servants instead of an annual appraisal. The Law on Ratification of the Agreement Establishing the Regional School of Public Administration was adopted in June 2010.

However, the legislative framework remains incomplete. The law on administrative procedures has not been adopted yet. The law on administrative disputes is not fully in line with European standards. Further efforts are needed to introduce a merit-based career system and effective human resources management. The capacity of the public administration in certain sectors is weak and coordination is not fully ensured. In view of an intensification of the EU integration process in the coming years, Serbia needs to further strengthen capacity on EU integration, in particular the central coordination between the General Secretariat, the Serbian EU Integration Office and in Ministry of Finance.

The various Ombudsman's Offices at both state and provincial level were very active. They reported an increase in the numbers of complaints, showing increased trust in the institution. In addition to dealing with individual cases, they proposed amendments to legislation, issued a number of opinions and recommendations, visited various institutions and organised activities aimed at promoting and protecting human and minority rights. Cooperation with local ombudsman's offices was also enhanced. In June 2010, the state Ombudsman opened a local field office in Southern Serbia. In Vojvodina, the Ombudsman and his two deputies were elected but the Vojvodina Ombudsman passed away in July and a new one was appointed in October 2010.

The Office of the Commissioner for Information of Public Importance and Personal Data Protection has stepped up its activities. Changes to the law on free access to information of public importance as of May 2010 introduced a mechanism for the enforcement of the Commissioner's decisions. They empower the Commissioner to impose fines on persons responsible for breaches of the law. However, the office still lacks permanent premises and suffers from staff shortages.

Concerning other independent regulatory institutions, the State Audit Institution has expanded in terms of both staff and office space. However, it has only performed a partial audit of the 2008 state accounts. The Competition Protection Commission, the Public Procurement Office and the Commission for the Protection of Bidders' Rights had difficulties in carrying out their duties owing to lack of resources and, in some cases, delays in the implementation of the relevant legislation.

Overall, the capacity of the public administration is good but reform in this area is advancing at a slow and uneven pace. Further improvement of the legislative framework and a stronger commitment to respect the mandate of independent regulatory bodies and provide them with adequate resources are needed.

Civilian oversight of the security forces

Parliament adopted six new legal acts in October 2009, completing the legislative framework for defence reform. These comprised the national security strategy, the defence strategy, the law regulating the military intelligence and military security agencies, the law on the military, labour and material obligations, the law on civilian service and the law on the use of the army and other defence forces in multinational operations outside Serbia. The law on civilian service replaced the previous government decree and regulated the constitutionally guaranteed right to conscientious objection. This also fulfilled one of Serbia's obligations under its Council of Europe

post-accession commitments. A section for cooperation with the EU was established in 2010 as part of the overall restructuring of the Ministry of Defence.

Parliamentary oversight of the security forces remains weak, however, as the legislature is not proactive and lacks capacity. The head of the parliamentary committee for security and defence was dismissed in March 2010 on abuse of office grounds. The committee has limited resources to deal with its wide scope of work, which covers internal affairs, defence and security.

The State Ombudsman carried out the first inspection of the state security agency in February 2010 to review the legality of measures with implications for human and minority rights. The overall assessment was that, in performing its functions that have an impact on human and minority rights, the agency abides by the legal order.

Overall, there was further progress towards completing the legislation providing for civilian oversight of security forces and implementing constitutionally guaranteed rights. However, civilian oversight, including the work of the relevant parliamentary committee, needs to be reinforced.

Judicial system

Serbia made little progress towards further bringing its judicial system into line with European standards, which is a key priority of the European Partnership.

The Law on the Judicial Academy was adopted in December 2009 and the Academy established as the body responsible for the vocational training and continued professional development of judges, prosecutors and judicial staff. New Court Rules of Procedure were adopted in December 2009. They regulate the work of courts and the internal organisation of the new court network. A new Law on Expert Witnesses was adopted in June 2010.

The reappointment procedure for all judges and prosecutors was carried out under the lead of the Ministry of Justice in the second half of 2009 and took effect as of January 2010. The overall number of judges and prosecutors was reduced by 20–25%. More than 800 judges were not reappointed, out of previously around 3.000 judges and misdemeanour judges.

A new structure of the court network was implemented as of January 2010. The 138 municipal courts were reorganised into 34 basic courts. In addition, there are 26 higher courts, 4 courts of appeal and the Supreme Court of Cassation. The organisation of the prosecution service was changed accordingly. The service was divided into basic, higher and appellate prosecution offices. Special departments exist for war crimes and for organised crime. The new Administrative Court became operational in January 2010. In July 2010, the appointment of members of the Constitutional Court was completed.

However, major aspects of the recent reforms are a matter of serious concern. The reappointment procedure for judges and prosecutors was carried out in a non-transparent way, putting at risk the principle of the independence of the judiciary. The bodies responsible for this exercise, the High Judicial Council and the State Prosecutorial Council, acted in a transitory composition, which neglected adequate representation of the profession and created a high risk of political influence. In addition, not all members had been appointed to either of the councils. Objective criteria for reappointment, which had been developed in close cooperation with the Council of Europe's Venice Commission, were not applied. Judges and prosecutors

were not heard during the procedure and did not receive adequate explanations for the decisions. First-time candidates (876 judges and 88 deputy prosecutors) were appointed without conducting interviews or applying merit-based criteria. The overall number of judges and prosecutors was not calculated in a reliable way and adjusted several times after the re-appointment had already been carried out. The right to appeal for non re-appointed judges was limited to recourse to the Constitutional Court, which does not have the capacity to fully review the decisions. Out of more than 1,500 appeals, only one case has been dealt with. In this case, the Constitutional Court, for procedural reasons, annulled the initial decision.

The High Judicial Council and the State Prosecutorial Council have not yet been elected in their permanent composition. New court presidents have not been appointed. The respective legal deadlines expired in July and March 2010. The planned new Criminal Procedure Code, the new Civil Procedure Code, the law on enforcement of judgments and the law on notaries have not been adopted.

The large backlog of pending cases remains a matter of concern, in particular as the recent reforms impacted negatively on the overall efficiency of the judicial system. The reduction of the number of judges and prosecutors was not based on a proper needs assessment. Under the new court system, courts which were closed continue to function as court units, in which civil cases are heard. This means that judges and judicial staff have to travel between courts and court units requiring significant resources and creating security concerns. A uniform system for organising the work of the court seats and the new court units has not been established. Case registration and the IT system connecting all courts and court units and allowing access to files are not fully operational.

The Constitutional court faces a backlog of some 7,000 pending cases, including the appeals filed by judges and prosecutors who have not been reappointed. The setting up of the Judicial Academy still is at an early stage and vocational trainings have not yet started.

Progress on domestic cases of war crimes continued to be slow. There are 20 ongoing court cases and investigations against 103 individuals.

Overall, Serbia's judicial system only partially meets its priorities. There are serious concerns over the way recent reforms were implemented, in particular the reappointment of judges and prosecutors.

Anti-corruption policy

Serbia made some progress in the fight against corruption. Implementation of the outstanding GRECO recommendations of June 2006 continued. Amendments to the Law on Civil Servants and the Law on Free Access to Information introduced the obligation for civil servants to report corruption and provided a certain protection from retaliatory measures. Also the access to information was improved. As regards the processing of corruption cases, there is good cooperation between the police and the state prosecution.

The new Anti-Corruption Agency started its work in January 2010. It is competent for preventive measures and the supervision of conflict of interest cases and funding of political parties. It received asset declarations from around 16,000 of the 18,000 officials who were required to submit such a declaration. The Agency maintains an asset register on its website. In March 2010, the Agency issued rules on the content of

records and financial reports of political parties. It maintained the earlier deadline of 15 April for parties to submit their annual reports and all parliamentary parties abided by the deadline.

The Anti-Corruption Council continued its advisory activities and raised public awareness of several high-profile cases.

However, implementation of the Action Plan was slow. There has been little progress in the investigation and prosecution of corruption cases, with the number of final convictions remaining low, in particular in high level cases.

The Anti-Corruption Agency is not yet fully staffed and lacks permanent premises and technical equipment. It still has to establish a track record of its capability to efficiently assess the correctness and completeness of asset declarations of public officials. In this respect, the Agency has little competencies on its own and remains dependent on the cooperation of other state bodies and the effectiveness of law enforcement authorities.

New legislation rendering the financing of political parties more transparent and providing for better control of expenditure has not yet been adopted. The existing legislation has significant shortcomings and does not provide the Anti-Corruption Agency with sufficient investigative and sanctioning powers to monitor party funding effectively, in particular during election campaigns.

Following efforts by the Anti-Corruption Agency to enforce the ban for officials to hold more than one public function, the relevant law was changed in July 2010 to partly suspend this ban. This raises concerns over the respect for decisions of the Agency and political will to support its work. The constitutionality of this suspension is subject to a case in the Constitutional Court.

Public procurement, privatisation procedures and public expenditure continue to be areas of serious concern, as independent supervision is not yet ensured. The setting up of the State Audit Institution remains slow and the first audit report produced covered only a small part of the state budget. Effective legal protection of whistleblowers is still missing, despite the newly introduced reporting obligation for civil servants. Protection is only applicable in cases where whistleblowers disclose information that is not classified. There is a lack of practical guidance on protective measures. Corruption within the police remains a matter of concern.

Overall, the institutional framework to fight corruption is in place with the Anti-Corruption Agency starting its work in January 2010. However, corruption remains prevalent in many areas and continues to be a serious problem. The legislative framework still shows shortcomings, in particular with regard to supervision of political party funding and the protection of whistleblowers. The Anti-Corruption Agency needs to be strengthened. Implementation of existing laws needs to be improved. Further efforts are needed to better process corruption cases, from investigation to final convictions.

2.2. Human rights and the protection of minorities

Observance of international human rights law

Concerning the *ratification of human rights instruments*, Serbia has signed and ratified all significant international instruments.

The *European Court of Human Rights (ECtHR)* delivered since October 2009 45 judgments finding that Serbia had violated the European Convention for the Protection of Human Rights and Fundamental Freedoms (ECHR). Over the same period, a total of 1364 new applications were made to the ECtHR. The largest number of judgments refers to the violation of the right to a fair trial due to the length of the procedure. As of September 2010, there were over 3,000 eligible cases pending before the ECtHR regarding Serbia.

There has been some progress in the *promotion and enforcement of human rights*. Several state bodies contributed to awareness-raising on human rights by organising various activities addressing issues relating to different human and minority rights. The Judicial Academy provided regular training on human rights standards for relevant professionals such as police officers, judges and prosecutors. However, the enforcement of the relevant ratified international agreements needs to improve. The State Secretary for human rights resigned in September 2010.

Overall, the legal framework for human rights protection is in place and generally respected. However, further efforts in education on international human rights standards and their implementation are needed.

Civil and political rights

There has been little progress in further improving the *prevention of torture, ill-treatment and the fight against impunity*. Police detention procedures are still of great concern, as well as the lack of internal and independent external oversight mechanism.

Additional efforts aimed at preventing any further cases of torture and ill-treatment are needed. The Deputy Ombudsman in charge of the protection of persons deprived of their liberty is operational but still not fully effective.

The obligation to establish a National Preventive Mechanism in accordance with the Optional Protocol to the Convention against torture and other cruel, inhuman and degrading treatment or punishment, has not yet been fulfilled.

The parliamentary commission provided for by the law on enforcement of criminal sanctions of 2006 has not yet been set up.

Access to justice is generally ensured, but there has been no further progress as legislation and funding for a more effective system of free legal aid is still missing.

Serbia made little progress in the reform of its *prison system*. A strategy to prevent overcrowding was adopted in July 2010. In order to address drug abuse, five 'drug-free' units were established. Efforts to provide training and adequate medical services to prisoners continued. However, poor conditions in prisons and in police detention facilities are of concern. Prisons remain significantly overcrowded with a prison population of over 11,000 for a capacity of 6,000 persons. This led to several protests and riots in prisons in 2010. Decisive action is needed to develop an efficient probation system and to introduce alternative sanctions on a broader scale. The availability and use of illicit drugs by prisoners and shortcomings in the provision of medical services remain of concern.

The general constitutional and legal framework for the protection of *freedom of expression* is in place and generally respected. However, incidents involving death threats, attacks and hate speech, in particular against journalists, have continued. The response of the police and prosecution has improved. However, further efforts are needed to ensure adequate follow-up by the courts. There is still no progress in the

investigation of the murders of journalists which took place during the 1990s and in 2001, and of the attempted murder of a journalist in 2007.

The legal framework generally allows the *media* to operate freely. In July 2010, acting on motions by the State Ombudsman and other organisations, the Constitutional Court ruled as unconstitutional several amendments to the Public Information Law, adopted in August 2009. The Court struck down the provision restricting the right of domestic legal persons to establish a public outlet, as well as the provisions which introduced heavy fines and other penalties.

Freedom of assembly is guaranteed by the Constitution and in general respected. Police response to acts of violence has improved. The acting state prosecutor filed a motion to the Ministry of the Interior to prohibit organised gatherings of extremist organisations of football fans following the murder of a French citizen in September 2009. The police took additional measures to prevent sport-related incidents and some matches were closed to the public. The police also prevented a rally by members and supporters of a neo-Nazi group in December 2009. The Belgrade Pride Parade took place in October 2010 thus representing a step forward in promoting constitutionally guaranteed fundamental rights. However, violent clashes occurred between the police and rioters protesting against the Parade. Rioters also targeted state institutions as well as ruling parties' premises. The response of the police was adequate and a large number of perpetrators were arrested.

Freedom of association is guaranteed by the Constitution and respected. The process of re-registration of existing political organisations and registration of new ones was completed in January 2010. 72 parties were registered, including 42 parties representing national minorities. 501 organisations that failed to abide by the new criteria were deleted from the register. Motions were filed by the state prosecution for the banning of two extreme right-wing organisations. The Constitutional Court started to process a motion filed by the acting state prosecutor in October 2009 to ban 14 sports fans organisations. This was on the grounds that their activities sought to violently overthrowing the constitutional order, violated human and minority rights and were an incitement to racial, ethnic and religious hatred.

Civil society organisations continued to be active in the social, economic and political life of Serbia and remain important in promoting democratic values. The Office for Cooperation with Civil Society was established by the government in April 2010. However, the Office is still not operational and cooperation between state authorities and civil society is still uneven. Legislation implementing the law on citizen's associations to prevent possible abuses regarding financing from the state budget is not yet adopted. Human rights defenders continued to be subject to harassment, verbal threats and physical attacks.

Constitutional guarantees providing for *freedom of religion* are in place and generally respected. In practice, the inter-faith situation has improved and fewer religiously motivated incidents were recorded. In February 2010, the long outstanding case concerning Jehovah's witnesses was settled and this organisation was registered. However, the 2009 annual report of the State Ombudsman identified an insufficient level of transparency and consistency in the registration process as the main obstacle to some smaller religious groups exercising their rights. Several cases, including the outstanding case of the Montenegrin Orthodox Church, are pending before the courts.

Overall, the constitutional framework providing for respect for civil and political rights is largely in place. However, full implementation and enforcement remain to be ensured. Relevant legislation remains to be brought more closely into line with European standards. Further action by the authorities in combating violence of all types is needed.

Economic and social rights

There has been some progress on economic and social rights.

Concerning *women's rights*, the law on gender equality, aimed at improving the position of women, was adopted in December 2009. Different projects and activities were carried out by Vojvodina provincial bodies and NGOs with a view to implementing Vojvodina's strategy for protection against domestic violence and other forms of gender-based violence. However, the action plan for the implementation of the National Strategy to improve the position of women and promote gender equality is still pending. In practice, women remain discriminated against, particularly in the labour market. Those facing the most discrimination are disabled women, single mothers, older women and those living in rural areas. There has been an increase in domestic violence. This situation remains insufficiently reported and the institutions responsible often fail to respond adequately to gender-based violence. The rules on legal protection of women during court proceedings are not sufficiently applied in practice.

In relation to *children's rights* there has been progress in strengthening the system for protecting children suffering from abuse and negligence. In May, the Ministry of Education adopted rules of procedure on violence in educational institutions aimed at replacing the separate protocols existing signed on this issue with relevant ministries. Various training programmes were implemented. Some aim at police officers, others at raising awareness among pupils in elementary schools. Two new shelters for street children were opened in Novi Sad and Nis. The parliamentary working group for children's rights, established last year with the aim of enhancing the role of parliament in improving the position of children, continues its activities. It regularly assesses all legislation, reports and other documents that affect children's rights.

However, in practice, there is a lack of follow up by state bodies of the requests for protection of pupils' rights in educational institutions. The rate of school attendance, particularly by Roma girls, is still of concern. There has been some progress towards inclusive education, but implementing legislation remains to be adopted. Amendments to the Family Law prohibiting corporal punishment are still pending. The revision of the national action plan for children, to include the protection of children from pornography and other forms of exploitation, is still awaited. Violence against children continues to be of great concern. Different measures available for the protection of children during court proceedings are not sufficiently implemented.

As regards *socially vulnerable persons and persons with disabilities*, the law on vocational rehabilitation and employment of disabled persons entered into force in May 2010. The process of de-institutionalisation for parentless children has continued. Initiatives have been taken to prevent institutionalisation, for example by promoting day care centres. However, both capacity and resources need to be strengthened.

In the area of *labour rights and trade unions*, the general agreement with the trade unions and the employers' associations continues to be suspended due to the economic crisis. In the private sector, the number of employees not receiving full wages or not

having social contributions regularly paid has been increasing. Social dialogue remains weak and consultation of social partners irregular. The Economic and Social Council is still not playing an active role in strengthening the social dialogue and remains rather marginalised, also including in the consultation process for legislation falling under its remit. Local councils still exist only in a small number of municipalities, and their role remains marginal.

The legislative framework prohibiting any kind of *discrimination* and establishing a mechanism for protection against discrimination is in place. The equality protection commissioner mandated to ensure full implementation of the law on the prohibition of discrimination was elected by parliament in May 2010 but is not fully operational yet. In practice, discrimination continues, particularly against the Roma, the LGBT community, women, national minorities, and persons with disabilities. These groups, but also human rights defenders and journalists, are exposed to hate speech and threats that are rarely followed up by the authorities.

With regard to *property rights*, the implementation of the law regulating private ownership of urban construction land adopted in September 2009 has been slow and inefficient. There has been little conversion of the right of usage into ownership of construction land. The issue of ownership over land acquired through the privatisation process has not been solved. The legal situation in this respect remains unclear. The announced legislation on restitution has not yet been adopted.

Overall, the legal framework for the protection of social and economic rights is broadly in place. However, the protection of women and children against all forms of violence needs to be ensured. Further measures fighting all kinds of discrimination remain to be introduced. Further efforts are required to clarify property rights.

Respect for and protection of minorities, cultural rights

Good progress has been made in the protection of minorities. The first direct elections for the National Minority Councils were held on 6 June 2010. The Councils have to be consulted on legislation relating to minority languages, education, culture and media. Councils were elected for 19 national minorities. Four national minorities formed and elected their councils for the first time. Both the number of registered voters and the turnout were relatively high. Elections were assessed by the OSCE as meeting international standards. Some irregularities and difficulties were reported, including during the registration process, although these did not significantly affect the overall results of the elections. The Councils are yet to become operational. Difficulties were experienced in the formation of the Bosniak National Minority Council which remains to be formally constituted.

In October 2009, the Republican Council for National Minorities held a session, due to a change in its composition. However, it has only met once. Information and education in minority languages remains to be improved and the relevant legal framework clarified. This is particularly the case for the Bosniak, Bulgarian, Bunjevci and Vlach minorities.

The inter-ethnic situation in *Vojvodina* continued to improve. The implementation of the new Statute and of the law on determination of competencies is ongoing. The adoption of new laws on public property and on provincial own resources is still pending. The overall number of inter-ethnic incidents has on the whole been decreasing. The provincial authorities continued organising regional youth camps to

promote tolerance. Regular cooperation and coordination has been established with the state authorities, in particular the Ministry of the Interior, and joint visits to vulnerable communities have been organised. Investigations by the police into inter-ethnic incidents has improved, as well as police sensitivity in treating them as ethnically motivated acts as opposed to the previous practice of classifying them as ordinary incidents. Their legal follow up has however been insufficient. The prosecution continued to dismiss them as criminal acts and referred them instead to misdemeanour courts. The 2009 annual report of the Provincial Ombudsman noted that out of 730 complaints received, 25 (3.42%) related to rights of national minorities.

The situation in *southern Serbia* was on the whole stable but tense. In October 2009, bilingual branches of the faculties of law and of economics were opened in Medvedja. The establishment of the task force intended to follow up the feasibility study on the development of higher education in Presevo and Bujanovac has been stalled. No sustainable solution has been found yet to the issue of the recognition of diplomas issued by the University of Pristina. The Albanian National Minority Council was established following direct elections. Tensions between Albanian political parties preceded these elections. The Council is however not yet fully active, since the parties have not been able to agree on distribution of posts. Some parties continue with the boycott of the council. An agreement was signed on the inclusion of Serbs in the local government in Bujanovac. A decision was made on opening additional vacancies in State institutions, which will allow for integration of Albanians in public administration. This decision remains to be implemented.

Clashes both between ethnic groups and within the Muslim community in *Sandžak* have continued. Tensions persist in particular between the two existing Islamic organisations. In September 2010, incidents occurred in Novi Pazar during a protest over a land dispute between the local Islamic organisation and the municipal authorities. The Bosniak National Minority Council, which members have been elected in June 2010, is not yet registered and fully functional due to a number of open issues related to its constitution.

There are approximately 83,000 *refugees* and 205,000 *internally displaced persons* (IDPs) in Serbia, according to the United Nations High Commissioner for Refugees. The number of collective centres has decreased. Changes were made to the law on refugees enabling refugees to buy out their apartments when these had been built from donations. The programme to support municipalities that prepared local action plans for the improvement of the status of refugees and IDPs who opt for local integration has continued. An additional 81 municipalities have received donations for the implementation of their plans. However, the situation of refugees and IDPs remains very difficult. Further improvement is needed to address the housing situation. Many refugees and IDPs are unemployed and live in poverty. The national strategy on refugees needs to be revised.

There has been some improvement in the position of the *Roma* population. Some affirmative action measures have been undertaken in the education sector with the goal of enhancing the status of Roma. Actions aimed at raising public awareness for Roma inclusion have been conducted on different occasions such as international Roma day. Action plans for the improvement of the status of Roma have been adopted in a number of municipalities. An additional 15 health mediators and 179 pedagogic assistants have been employed during reporting period.

However, the Roma minority continues to face discrimination. Most Roma people live in extreme poverty and illegal settlements. Problems with access to personal documents persist for Roma people living in illegal settlements without a registered address or who are homeless. A simplified procedure for recognition of legal subjectivity and subsequent registration in citizens' registries has not been introduced yet. This adversely affects the exercise of their social and economic rights. Relocation of illegal Roma settlements is often conducted inadequately, resulting in breaches of basic human rights. The Roma population, especially Roma women, are discriminated in the labour market and only 5% of the Roma population have a permanent job. Roma women and children are frequently subject to exploitation and family violence, which often passes unreported.

Overall, the legal framework on the respect for and protection of minorities in Serbia is in place. The National Minority Council elections were on the whole successfully organised. Some improvements were recorded towards addressing the issue of the status of refugees and IDPs. However, the National Minority Councils are yet to become operational. The number of IDPs remains high and their situation critical. The majority of the Roma population lives in extreme poverty and continues to face discrimination in particular as regards access to education, social protection, health care, employment and adequate housing.

2.3. Regional issues and international obligations

There are no outstanding issues in connection with Serbia's compliance with the *Dayton/Paris peace agreement*. Serbia has demonstrated a constructive approach in connection with developments in Bosnia and Herzegovina.

The Prosecutor of the *International Criminal Tribunal for the former Yugoslavia (ICTY)* noted in his latest report to the UN Security Council that Serbia's responses to the Office of the Prosecutor's requests for access to documents, archives and witnesses have been timely and adequate and that no requests remain outstanding. He also stressed the professionalism and commitment of the operational services working on the search for fugitives. The report however recommended that Serbia review the strategies employed to apprehend the remaining fugitives, Ratko Mladić and Goran Hadžić. The need for an increase in Serbia's operational capacities and the adoption of a more rigorous and multi-disciplinary approach to arresting the fugitives was also highlighted by the ICTY report. Full cooperation with the ICTY remains an essential condition for membership of the EU, in line with the Council conclusions of 25 October 2010.

The status of the former State Union Law on the freezing of assets of ICTY fugitives, which was adopted in 2006, has not yet been clarified. In practice, the freezing of assets has been implemented on the basis of a decision made in 2005 by the war crimes chamber of the Belgrade District Court. The legal basis for this decision was the Criminal Procedure Code.

Good cooperation with EULEX has been established in relation to *war crimes* in Kosovo.³ The investigative capacity of the police in war crimes was hampered by the lack of expert staff such as military analysts and intelligence officers. This adversely

³ Under UNSCR 1244/99.

affected the quality of the work of relevant services. Problems of extradition and recognition of sentences with some countries of the region continued to exist.

Serbia's policy regarding the *International Criminal Court* continues to be in line with the

EU's guiding principles and the EU Common Positions on the integrity of the Rome Statute.

The Serbian government has continued to contest Kosovo's declaration of independence. The case before the International Court of Justice (ICJ), initiated by Serbia, came to an end in July 2010 with the issuing of an advisory opinion. The Court concluded that the declaration of independence of Kosovo adopted on 17 February 2008 did not violate general international law and the UN Security Council Resolution 1244 (1999). The Serbian parliament consequently adopted by an overwhelming majority a decision reiterating Belgrade's policy of non-recognition of Kosovo and supporting the government's initiative to have the issue referred to the UN General Assembly. Serbia has also maintained its opposition to the participation of Kosovo in regional meetings and initiatives other than under the UNMIK umbrella.

The UN General Assembly adopted on 9 September a joint resolution tabled by Serbia and co-sponsored by the EU as a follow-up to the ICJ advisory opinion on Kosovo. The resolution acknowledged the content of the ICJ advisory opinion and welcomed the readiness of the European Union to facilitate a process of dialogue between the parties; the process of dialogue in itself would be a factor for peace, security and stability in the region, and that dialogue would be to promote cooperation, achieve progress on the path to the European Union and improve the lives of the people.

In Kosovo, Serbia maintained parallel structures and organised parallel municipal by-elections. Serbia also discouraged Serb participation in the municipal elections organised by the Kosovo authorities in November 2009. Serbian officials visiting Kosovo continued to give prior notification to UNMIK and EULEX for the purpose of obtaining security escorts. Serbia failed to play a constructive role in the return of Kosovo Serb and Kosovo Albanian judges and prosecutors back to Mitrovica District Court, which remains staffed only by EULEX personnel. The Serbian government protested against the disconnection and dismantling of the Serbian mobile phone transmitters in Kosovo which had operated without a licence.

The policy on Kosovo has also affected Serbia's bilateral relations with its neighbours. The Serbian government still does not accept the Kosovo customs stamps notified by UNMIK, blocking Kosovo's exports to Serbia and hampering transit of Kosovo goods for export to the EU by EU hauliers.

In August 2010, a total of 14,631 persons were still missing as a result of the conflicts in the region. Of these, 10,402 cases were related to the conflict in Bosnia and Herzegovina; 2,392 to the conflict in Croatia and 1,837 to the conflict in Kosovo according to figures provided by the Red Cross (ICRC). The process for solving these cases has been very slow. Solving these remaining cases within a reasonable time limit is essential for the reconciliation process. The working group set up between Belgrade and Pristina met three times under ICRC auspices, but progress on resolving cases has slowed because of the lack of information on gravesite locations. In 2010, the Serbian Commission for Missing Persons received for the first time copies of documents from the archives of the Serbian Ministry of Defence in response to detailed requests for information submitted by the ICRC on persons who went missing in Kosovo in 1998

and 1999. The Serbian Police also provided the ICRC-chaired working group with new information from its own archives. The Belgrade-Pristina working group met in May 2010 and discussed a newly discovered location on the territory of Serbia that is suspected of being a mass grave. The Serbian war crimes prosecution proposed opening an investigation into this matter. The Commission on Missing Persons – a bilateral forum set-up between Belgrade and Zagreb to deal with the issue – meets only irregularly.

Fresh impetus was given to the *Sarajevo declaration process* following the Ministerial meeting held in Belgrade in March 2010, at Serbia's initiative. This brought together Bosnia and Herzegovina, Croatia, Montenegro and Serbia, all of which agreed to work together in order to clarify refugee statistics. The countries also committed themselves to work towards solutions to a number of outstanding issues by the end of the year. However, there are a number of difficult issues, in particular that of occupancy and tenancy rights, which still need to be tackled with the objective of finding mutually acceptable solutions. The Sarajevo Process was initially launched through the Sarajevo Declaration of January 31, 2005. Bosnia and Herzegovina, Croatia, Montenegro and Serbia cooperate within this process to find solutions for refugees and other persons who were displaced as a result of the armed conflicts in ex-Yugoslavia between 1991 and 1995.

Regional cooperation and good neighbourly relations form an essential part of Serbia's process of moving towards the European Union. The Serbian government has declared regional cooperation one of its priorities. Serbia continued to be an active participant in regional initiatives, including the South East European Cooperation Process (SEECP), the Regional Cooperation Council (RCC), the Central European Free Trade Area Agreement (CEFTA), the Energy Community Treaty (ECT) and the European Common Aviation Area Agreement (ECAA). Serbia participated in the technical negotiations for the Transport Community Treaty, the signing of which has been delayed over differing positions on Kosovo. Serbia held the Chairmanship of CEFTA in 2010. Serbia has been actively participating in the preparations for the forthcoming Danube Strategy. Serbia participated in the EU-Western Balkans High-Level Meeting that took place in June 2010 in Sarajevo. However, regional cooperation was affected by a lack of agreement between Serbia and Kosovo on the latter's participation in various regional meetings. An acceptable and sustainable solution for the participation of both Serbia and Kosovo in regional fora needs to be agreed as soon as possible. This is essential for inclusive and functioning regional cooperation.

Trilateral meetings took place in 2009 between Turkey, Serbia and Bosnia and Herzegovina. In April 2010, the heads of state of Serbia and Turkey, and the Chair of the Presidency of Bosnia and Herzegovina signed a Declaration in Istanbul endorsing the territorial integrity, sovereignty and legal personality of Bosnia and Herzegovina.

President Tadić, together with the Chair of the Presidency of Bosnia and Herzegovina and the Presidents of Croatia and Montenegro, attended the May 2010 summit of the Igman Initiative in Sarajevo. This year marked the 10th anniversary of this initiative involving more than 140 NGOs from the region which is aimed at promoting and facilitating local and regional cooperation.

Bilateral relations with other enlargement countries developed further. Judicial cooperation in penal matters has improved between Bosnia and Herzegovina, Croatia and Serbia. Serbia signed an agreement with Bosnia and Herzegovina in February on

mutual recognition and enforcement of court rulings in criminal matters. The new agreements introduce the possibility of forced transfers of convicted persons to serve imprisonment. The convicted person could, according to the previous agreements, not be transferred from a country where he had a citizenship without giving his consent. The new bilateral agreements put an end to this possibility to escape imprisonment, in particular for persons with dual nationality.

There was good progress in relations with *Albania*. In March 2010, the Albanian Minister of Foreign Affairs visited Belgrade for the first visit of this kind in five years. On this occasion, an agreement on cooperation in fighting organised crime, international drug trafficking and international terrorism was signed. As a follow-up to this visit, in April 2010 Albania abolished visas for Serbian citizens.

Relations with *Bosnia and Herzegovina* have improved. The Serbian parliament adopted in March 2010 a Declaration condemning the crime in Srebrenica and referring to the International Court of Justice ruling on Srebrenica. The preamble to this Declaration also restates the commitment to respect the territorial integrity and sovereignty of Bosnia and Herzegovina. President Tadić attended in July 2010 the Srebrenica commemoration. The Speaker of the Bosnia and Herzegovina House of Peoples met the President of Serbia in Belgrade in June. A new ambassador from Bosnia and Herzegovina was accredited after the post had been vacant for three years. In March 2010 the Serbian parliament ratified the agreement on determination of border crossings with Bosnia and Herzegovina. The Inter-State Cooperation Council for the border between the two countries met in May 2010 for the first time after four years. The Economic Cooperation Agreement between Bosnia and Herzegovina and Serbia entered into force in April. Amendments to the agreement on mutual legal assistance in criminal matters were signed in February 2010. A bilateral agreement on police cooperation in areas such as organised crime and terrorism was signed, as was an agreement on culture and sport. However, border demarcation remains an open issue. Republika Srpska continues to cooperate closely with Serbia on the basis of the Special Parallel Relations Agreement and the related Protocol on Cooperation.

Relations with *Croatia* have gained a fresh impetus. Following the election of President Josipović in Croatia, the two Presidents and other senior officials met several times, both bilaterally and in the margins of regional and international events. A Serbian parliamentary delegation visited Zagreb in February 2010 and a return visit was made by the Croatian parliament in June 2010. The Croatian President visited Serbia in July 2010. The inter-state border commission met in April 2010 for the first time in seven years. A Police Cooperation Agreement entered into force in May 2010. A defence cooperation agreement and an agreement on inland water navigation were signed. An agreement for the extradition of citizens suspected or convicted of serious crimes was signed in June 2010. However, outstanding issues remain. In December 2009, the Serbian government lodged a counter-suit against Croatia in the ICJ on the grounds of genocide allegations. The issue of missing persons is still problematic.

Relations with the *former Yugoslav Republic of Macedonia* are overall good. The President of Serbia visited Skopje in June 2010. The Serbian authorities maintained their policy of non-recognition of the border demarcation agreement between the former Yugoslav Republic of Macedonia and Kosovo. In September the countries signed a bilateral agreement to facilitate traffic over the local border crossing points. Unresolved issues concerning relations between the Orthodox churches in the two countries remain.

There were mixed trends in relations with *Montenegro*. The Serbian President visited Montenegro in July 2010. An agreement on cooperation in the military sector was signed by the two Ministers of Defence in April 2010. The Serbian government protested over the establishment of diplomatic relations between Montenegro and Kosovo and temporarily recalled its ambassador from Podgorica in January 2010. The ambassador returned in February 2010. There were also outstanding issues in connection with the finalisation of the distribution of assets and liabilities, citizenship rights, and the fight against organised crime. Agreements on judicial cooperation and extraditions were ratified by Serbia in May 2010, but do not provide for the extradition of own nationals.

There was significant progress in relations with *Turkey*. The new format of regular trilateral meetings at the level of Ministers of Foreign Affairs with Turkey and Bosnia and Herzegovina was launched in 2009 and several meetings took place. The summit of the Presidents of Serbia, Turkey and of the Bosnia and Herzegovina Presidency took place in Istanbul in April 2010. The Turkish Prime Minister visited Serbia in July 2010. The Serbia- Turkey free trade agreement entered into force in September 2010.

Relations with *Romania, Bulgaria and Hungary* are good. In April 2010 the Bulgarian Prime Minister visited Belgrade. The Serbian and Bulgarian Interior Ministers signed an agreement on the establishment of a joint contact centre for police and customs cooperation. High-level meetings with Hungary took place at bilateral level and in the new trilateral format of cooperation with Hungary and Croatia. In June 2010 the Romanian Minister of Foreign Affairs visited Belgrade. The two countries also maintain a high level of cooperation between their police departments.

Overall, Serbia's international obligations are broadly complied with. Despite the active on-going cooperation of Serbia with ICTY, the two remaining fugitives are still at large. Domestic processing of war crimes cases continued. Regional cooperation has improved and Serbia made significant progress in its bilateral relations with other enlargement countries, particularly Croatia and Bosnia and Herzegovina, while continuing to have good relations with neighbouring EU member states. Regional cooperation was affected by a lack of agreement between Serbia and Kosovo on the latter's participation in regional meetings. An acceptable and sustainable solution for the participation of both Serbia and Kosovo in regional fora needs to be agreed as soon as possible. This is essential for inclusive and functioning regional cooperation.

3. ECONOMIC CRITERIA

In examining economic developments in Serbia, the Commission's approach was guided by the conclusions of the European Council in Copenhagen in June 1993, which stated that membership of the Union requires the existence of a functioning market economy and the capacity to cope with competitive pressure and market forces within the Union.

3.1. The existence of a functioning market economy

Economic policy essentials

In January 2010, the government submitted to the European Commission its economic and fiscal programme for the period 2010-12. The programme sets out a revised macroeconomic and fiscal policy framework for the medium term based on the

supplementary budget for 2009 and the 2010 budget that were both adopted by parliament in December 2009. *Overall*, the programme is an appropriate medium-term policy document, presenting a realistic macro-fiscal scenario that is broadly consistent with the country's reform agenda.

Serbia's macroeconomic policy has been anchored by the economic programme supported by the International Monetary Fund (IMF) under the Stand-By Arrangement (SBA) since early 2009. Pursuant to the SBA requirements, a number of fiscal measures were implemented throughout 2009 and in early 2010. Notwithstanding a number of adjustments, including an upward revision of fiscal deficits in 2009 and 2010, the SBA has been on track. The government made significant strides towards enhancing fiscal responsibility by adopting amendments to the budget system law and a new pension bill. However, comprehensive structural reforms that would gear the economy towards a more sustainable path will need to be further pursued and implemented.

Overall, macroeconomic stability was broadly preserved against the backdrop of the global crisis owing to the adoption of timely measures in agreement with the IMF. There is consensus on the fundamentals of a market economy. Medium-term fiscal and structural reforms will have to be implemented without delay to enhance the resilience of the economy.

Macroeconomic stability

In 2009, Serbia's GDP shrank by 3% in real terms as a consequence of the global economic crisis, interrupting a period of steady growth with an annual average rate of 6% recorded between 2005 and 2008. The 2009 average per capita GDP in purchasing power standards stood at 37% of the EU-27 average, up marginally from the year before. The recovery has been under way since early 2010 but the pick-up in economic activity has been slower than expected, prompting the IMF and the national authorities to revise downwards their initial GDP growth projection from 2% to 1.5%. While economic growth in the past was driven by domestic demand, it has been recently fuelled more by export expansion. This shift remains to be sustained, based on the strengthening industrial production. While in 2009 industrial output was some 12% lower than the year before, with manufacturing recording the sharpest fall, the negative trend has reversed in 2010. *Overall*, the Serbian economy continues to be affected by the global economic crisis while recovery has been slow and fragile. In 2009, international trade and financial transactions were significantly affected by the global economic and financial crisis. At 5.8% of GDP, the current account deficit was considerably lower compared to levels of 10-18% in previous years. This was mainly due to a sharp decline in imports as well as an increase in net inflows of remittances. As imports fell faster than exports the merchandise trade deficit also narrowed as compared to past levels of above 20%. However, at 15.5% of GDP it remained substantial. In 2010, as the international economic environment improved, Serbia's external position stayed solid. In the period to September, the trade deficit was narrowing compared to last year on the back of vigorous export growth as exports of intermediate goods soared following the revived industrial activity in the EU, Serbia's main trade partner. Annual import growth turned positive in May following a marked pick-up in imports of energy, partly due to the higher international oil prices, and intermediate goods against the backdrop of a gradual recovery in domestic production while investment activity was subdued.

Financial and capital flows remained modest. In 2009, foreign direct investment (FDI) fell by a quarter compared to a year earlier, to €1.37 billion, accounting for 4.3% of GDP. At the same time, long-term borrowing by the corporate sector at €600 billion was only a quarter of the 2008 level while short-term borrowing at €200 million was down by almost 60% on the year before. Notwithstanding the slowly recovering economic activity as of 2010, foreign currency inflows have remained subdued. Over the eight months to September, FDI and other investments were substantially lower than a year ago. The capital and financial account increased as a consequence of domestic commercial banks resorting to additional long-term borrowing while hefty repayments by corporate sector of the pre-crisis foreign loans and an outflow of cash and deposits have been taking place. Still, total foreign exchange reserves remained largely stable during 2010 at over €11 billion, i.e. more than a third of GDP or sufficient to cover some 10 months' worth of imports. Serbia's foreign debt has been increasing since 2009 while capital inflows have been largely insufficient to cover the current account deficit. By end-July 2010, gross external debt had risen by around €0.5 billion since the beginning of the year, to €23.3 billion, i.e. close to 80% of projected GDP. *Overall*, the Serbian economy saw a substantial external adjustment in 2009 reflected in a considerably narrower current account deficit as well as a lower merchandise trade deficit compared to past levels. In parallel, foreign exchange reserves were built up and are now maintained at a comfortable level. External debt is, however, high and growing indebtedness remains an issue of concern.

The unemployment rate in 2009 increased to 16.1%. 2009 saw significant wage moderation owing also to the nominal freezing of salaries in the public sector, with nominal wages increasing by 6.9% on average compared to 17.9% a year earlier. Moreover, real wage growth slowed to only 0.3% per annum, which was substantially lower than in 2007 (19.5%) and 2008 (3.9%). While economic activity has been picking up gradually, the situation on the labour market has worsened in 2010. In the first half of the year, employment continued to fall in annual terms, with the number of employed persons dropping to historic lows at 1.85 million. According to the national labour force survey of April 2010, the unemployment rate soared to 19.2%. The poor labour market performance has further undermined the social conditions. Wage growth has remained broadly constrained during 2010. In the period from January to July, the average net wage increased compared to the same period last year, by 6.7% in nominal and 2.5% in real terms. *Overall*, under the impact of the economic crisis labour market conditions deteriorated as employment fell and unemployment approached 20%. Salaries remained almost unchanged in real terms.

The current monetary policy framework has been in place since January 2009 when the National Bank of Serbia (NBS) committed itself to price stability based on consumer price index (CPI) inflation instead of core inflation. The NBS's target was to keep annual CPI inflation between 6% and 10% throughout 2009. At end-December 2009, CPI inflation stood at 6.6%, largely in line with the projections, bringing the yearly average inflation rate of 8.1% well within the target band. In 2009, inflation was largely fuelled by an increase in administered prices of oil derivatives and communal services. For the end of 2010, the NBS set the inflation target band at between 4% and 8%, where the main contribution to overall price growth would come from the rise in regulated prices and excise duties. Disinflation was on track in the first half of the year. However, inflationary tensions were rekindled by rising food prices and the dinar depreciation. The renewed pressures were also based on the expected strengthening of

domestic demand in line with the gradual pick-up of economic activity and higher bank lending. The acceleration of inflation prompted the NBS to discontinue the course of a gradual relaxation of monetary conditions. Since the second half of 2009, the key reference interest rate was cut in a number of consecutive steps from its October 2008 peak at 17.75% to 10% by end-December 2009, and further to 8% by early May. Following the two latest rate hikes, the interest rate currently stands at 9%. *Overall*, disinflation has remained the key policy objective, but price developments need to be monitored carefully as further inflationary pressures might be generated by the increases in regulated prices of energy, gas and oil as well as the pass-through effect of the depreciating dinar.

Since late 2009, the NBS has been actively engaged in preserving exchange rate stability. As the pace of the dinar depreciation in December 2009 was deemed to undermine the process of economic stabilisation, the NBS started intervening again in the interbank foreign currency market. After two interventions at the end of the year, the operations became more frequent in 2010, especially from mid-May when the pressure on the exchange rate again intensified. Despite the NBS's interventions, the dinar continued to slide, rising to RSD106.2 per euro at end-September, i.e. losing about 10% of its value since the beginning of the year. By then, the NBS had sold more than €2 billion in total with the aim of buffering extreme daily fluctuations in the dinar's value. *Overall*, the dinar has been on a depreciating trend since December 2009. In line with the policy of preventing excessive volatility of the exchange rate, the NBS's interventions on the interbank market were considerable in the first half of 2010 and have, in practice, somewhat overshadowed its inflation targeting policy.

The year 2009 saw a shift in the fiscal stance as the expansionary policy of 2007 and 2008 became constrained by the SBA programme requirements. *Ad hoc* short-term measures were introduced to mitigate the sharp deterioration of public finances during the economic recession, resulting in two 2009 budget revisions. The consolidated fiscal deficit in 2009 widened to 4.1% of GDP from 2.4% of GDP a year earlier. A set of emergency expenditure measures only partly compensated for the sizeable revenue shortfall. The fiscal adjustment came largely from restricted hiring in the public sector and a nominal freeze on public sector wages and pensions. Capital expenditures were again reduced in comparison with a year earlier. Extensive lay-offs in the private sector and salary freezes in the public sector translated into a shortfall in personal income tax revenue. Furthermore, VAT plunged due to restrained domestic demand. Because of the drop in imports and also the lowering of tariffs following the start of implementation of the trade agreement under the SAA, customs revenues were much lower compared to past years. Conversely, excise taxes increased as a consequence of the hike in excise duties on diesel and gasoline. During 2010, public finances remained under pressure as the fiscal policy allowed automatic stabilisers to operate. In agreement with the IMF, Serbia announced a supplementary budget to allow for a higher budget deficit in 2010. At 4.8% of GDP, the deficit would be the highest in the past decade, but driven by lower-than-planned public revenue rather than growing public expenditure. However, in the period to September public spending was contained largely through a significant cut in capital expenditure, while current expenditure, accounting for the bulk of total outlays, was in line with the plan against the freeze of public administration salaries and pensions. As of 2009, public debt has been increasing steadily and stood at close to €11 billion, i.e. some 36% of GDP, at end-August. With the aim to strengthen fiscal discipline, Serbia adopted the

amendments to the budget system law. These amendments introduce a set of quantitative fiscal rules to underpin fiscal consolidation over the medium term. Furthermore, improved procedures as well as the setting-up of a fiscal council are deemed to anchor fiscal responsibility. However Serbia still needs to adopt the new pension law which, for the purpose of strengthening public finances in the long run, includes an extension of working period and age for assuming pension rights as well as adjustments to the indexation mechanism. *Overall*, given the adverse impacts of the economic crisis and despite the *ad hoc* fiscal adjustments, the 2009 budget deficit was substantially higher than in previous years. The corrective short-term measures will need to be backed up by full-fledged systemic reforms, such as reform of the pension and healthcare systems, to improve fiscal sustainability in the medium to long term.

Expansionary fiscal policy and the increasing gap between savings and investment of the private sector, which fuelled external imbalances in the years prior to the 2009 economic downturn exacerbated the economy's vulnerabilities to adverse shocks such as a global recession. The negative effects of the last crisis have been partly cushioned by the economic measures implemented under the IMF SBA programme. However, the macroeconomic policy mix has proven rather limited in responding to the crisis. Effectiveness of monetary policy has been restricted given the high degree of euroisation and the NBS effectively pursuing dual objectives, i.e. smoothing the exchange rate depreciation while being committed to inflation targeting. Moreover, counter-cyclical fiscal policies, which would have been necessary in the period of low economic activity, could not be implemented. This was due to the pre-crisis fiscal expansion and the low capital market integration. To broadly preserve the stability of its economy, Serbia had to apply budget tightening measures, including expenditure cuts, which tend to operate pro-cyclically in such circumstances. *Overall*, the economic policy mix in place has proven limited in facing the crisis. However, the accompanying policies and measures agreed with the IMF under the SBA programme have provided an adequate response towards the most pressing negative macroeconomic effects.

Interplay of market forces

The price liberalisation process slowed down in 2009, with the share of administrative prices still representing about a quarter in the CPI inflation basket. The market formation of prices was challenged in mid-2010 as the state intervened following the shortage of basic food items such as dairy and cooking oil. The share of the private sector remained small, accounting for 55-60% of total output and about 60% of the total number of employees. Finalisation of the process of privatisation and/or liquidation of socially and state-owned enterprises remains one of the key priorities of the European partnership for Serbia.

Privatisation of the socially owned companies continued in 2009 but at a slower pace as only 95 such companies were sold. Privatisation proceeds amounted to about €81 million. By the end of 2009, the total number of companies privatised through tenders and auctions, since the start of the process in 2002, had risen to over 2,300, with privatisation revenue totalling about €2.6 billion. The least attractive companies remain unsold. The number of privatisations annulled — due to non-compliance with the contracted obligations — rose to almost one quarter of the firms initially scheduled for privatisation. The government extended the deadline for finalising privatisation of the socially owned companies to 30 June 2011. *Overall*, progress in selling socially

owned companies was limited, while the number of revoked privatisation deals increased.

Given the economic circumstances in 2009, privatisation of the large state-owned companies was delayed. As the situation in the global markets gradually improved, the government announced privatisation strategies for a number of companies. A few were slated for sale by the end of 2010. Privatisation of the pharmaceutical company Galenika failed, however, and has been postponed. The initial procedures were launched for the telecoms incumbent Telekom but the tender had not been called by the end of September, as planned. As regards the sale of the national air carrier JAT Airways, the government decided to establish a new national airline company that will take over the assets and some of the staff. The debt estimated at €146 million (€25 million in 2009 alone) would be left to the old company, which will remain in state ownership. To facilitate the sale of the remaining state-share in the oil company NIS, the government distributed free shares to the population in mid-2010 and announced further distributions (Belgrade Airport, Telekom, the electricity operator EPS). Privatisation of about 500 utilities in the local communities is outstanding. Their restructuring and reorganisation has not yet begun and the strategy for privatising them remains undefined. *Overall*, limited progress was made in finalising the privatisation process. Privatisation of socially owned companies has advanced but in the meantime a number of privatisation deals have also been cancelled. State-owned companies have not initiated the restructuring.

Market entry and exit

In 2009, some progress was made in facilitating market entry. The number of registered companies stood at 113,000 in May 2010, up from 106,000 in April 2009. At the same time, about 225,000 entrepreneurs were registered with the Serbian Business Registry Agency, i.e. around 5,000 more than a year earlier. The one-stop-shop system for registering a company has been in place since May 2009. It now takes on average 5 instead of 23 days to register and has been estimated to significantly lower administration cost for companies. The Agency has also further extended the number of registers, including the Registry for Financial Statements, which will do away with the past practice of multiple submissions of these statements to various state bodies. Nevertheless, further efforts are needed to improve the conditions for starting-up a business, particularly in the area of construction permits, where implementation of the new Law on planning and construction from 2009 has been very slow. With regard to market exit, a new Bankruptcy Law came into effect in January 2010 but the number of pending cases remains very high. *Overall*, there has been some progress, particularly regarding the registration of new companies and submission of the financial statements of those already operating. However, excessive red tape and complex legislation remain in place and continue to hamper the business environment.

Legal system

Some progress was observed in adopting new legislation in line with the *acquis*. However, preparation and implementation of the laws are sometimes slow and uneven. Also, legal enforcement is weak due to technical and personnel shortcomings in the courts and administrative bodies. Inconsistent implementation of laws and very lengthy procedures, which frequently exceed the deadlines set by law, hinder investment. *Overall*, weaknesses in the rule of law and prevalent corruption continued

to limit legal predictability and undermined trust in the legal system among economic operators, in particular as regards effective enforcement of property rights.

Financial sector development

The number of banks decreased from 34 to 33 after the merger of two state-owned banks in September 2010. There are now 3 majority state-owned banks, holding a 2.6% market share. Foreign ownership has risen to almost 75% of the total banking sector and currently 21 out of 33 banks operating in Serbia are owned by foreign entities. Subsidiaries of Austrian, Greek and Italian banks are within the top five banks in terms of assets and together control almost 60% of the market. Domestic private banks are small with only one of them among the top 10 banks.

Serbia's financial sector has been relatively unscathed by the international financial crisis. In line with the agreement reached in March 2009 ('Vienna Initiative'), the parent commercial banks having subsidiaries in Serbia maintained their exposure in the Serbian market at the pre-crisis level and effectively increased their capital adequacy ratios in 2009. Given the positive results of the economic stabilisation programme, it was agreed that exposure commitments could be reduced as of April 2010, from 100% to 80% of the end-2008 exposure as a first step towards phasing-out of the initiative. Deposits, of which 70% are in foreign currency, represent almost 60% of the total liabilities of the banking sector. Similarly, loans account for some 60% of banking sector assets. Over three quarters of loans are denominated in foreign currency or are foreign-currency linked, predominantly in euros. More than half of the loans are granted to the corporate sector (mainly to trade and industry — around 20% each) while about a third is for households. Since the crisis credit growth for the private sector has decelerated substantially and the government has put in place a support scheme to subsidise commercial bank loans to companies and households.

Capitalisation of the banking sector is high. The average capital adequacy ratio stands at 21% while all systemic banks maintain it above the prescribed minimum of 12%. However, the asset quality of the banking sector has worsened, with a rise in bad loans since 2009. The gross non-performing loans ratio peaked at 17.5% by the second half of 2010. A systemic liquidity crisis is unlikely as liquid assets accounted for over 36% of total assets at end-June. The NBS can release ample amounts of liquidity by further relaxing relatively high reserve requirements, which were introduced with the aim to limit rapid credit growth prior to the crisis. The high capital and reserve requirements have been partly responsible for the generally low profitability of the Serbian banking sector by regional standards. Stress tests for 31 banks carried out in 2010 concluded that banks are sufficiently resilient to further adverse shocks but remain vulnerable to credit risk. The weak performance of the corporate sector in the face of the slow economic recovery may raise defaults in the servicing of loans. Furthermore, there is some exchange rate risk on the borrowers' side given the high degree of euroisation of Serbia's economy. *Overall*, financial intermediation growth has slowed down against the backdrop of the economic downturn. The banking sector remained generally sound and profitable, but a close watch needs to be kept for possible deterioration in the repayment capacity of borrowers due to the relatively high share of bad loans and considerable exposure to exchange rate risk.

At the end of 2009, there were 26 insurance companies operating in Serbia, up from 24 a year earlier. 19 insurance companies are in majority foreign ownership while 7 rely on predominantly domestic capital. The recession has impacted the performance

of the sector, with premium income having risen only by 2.6% on the year in 2009. The insurance sector's share of capital in the total financial sector dropped to 3.9%. *Overall*, progress in development of the non-banking financial sector slowed down and consequently its size in financial intermediation remained limited.

3.2. The capacity to cope with competitive pressure and market forces within the Union

Existence of a functioning market economy

The overall economic climate deteriorated in the face of the global crisis but the authorities have succeeded in broadly maintaining macroeconomic stability to support the continued transition to a market economy. In particular, the monetary authorities applied timely and adequate measures to restore trust in the banking system. On the fiscal side, the corrective short-term measures will need to be backed up by full-fledged systemic reforms to ensure fiscal sustainability in the medium to long term. The adoption of the fiscal responsibility legislation is an important step, which paves the way towards bolstering fiscal discipline. Pension reform will also contribute will also contribute to the long-term sustainability of public finances. However, the weak corporate governance and the deficiencies in competition continue to be barriers to business. *Overall*, in the more challenging environment the previously identified handicaps have become more acute. Market mechanisms remained hampered by distortions, legal uncertainty, heavy state involvement in production, and insufficient competition.

Human and physical capital

Some progress was observed following the accelerated reform of the education system, which is poised to better meet labour market demand. Nevertheless, the gap between demand for and supply of skilled workforce identified in previous reports continues to be a drag on FDI and the development of new segments of the economy. The attitude towards lifelong learning and mobility has been improving, albeit at a rather slow pace. Public education expenditure accounted for 3.3% of GDP in 2009, lower than the planned 3.9%. *Overall*, the economy continues to suffer from a shortage of skilled labour while supply has been only gradually adjusting to market needs.

In 2009, investment activity was constrained and the private investment rate dropped to 20% of GDP. Net FDI fell by almost 25% on the year before, to €1.37 billion, bringing the cumulative inflow since 2000 to €12.2 billion. The three sectors receiving most FDI were financial intermediation, manufacturing, and transport and telecommunication. However, a large share of FDI was destined to the non-tradable sectors of the economy, which contributed to the increasing external imbalances. In 2009, domestic investment dwindled. The funds of the National Investment Plan were slashed to €210 million, a third of the 2008 amount, and were used for various projects related to the development of communal and road infrastructure in the 40 least developed municipalities but also in support of industrial hubs (such as Kragujevac) along Corridor X, as well as for construction of social housing. For 2010, the National Investment Plan was further reduced to about €100 million. *Overall*, domestic investment has been declining as local sources have been scarce and FDI has also lost momentum given the globally unfavourable economic conditions.

Sectoral and enterprise structure

The restructuring process has advanced only slowly. The shift of economic activity towards the service sector has stabilised, with services contributing more than 60% of GDP. The public companies still generate a large part of Serbia's output. However, their performance has been undermined considerably by the crisis, with the erosion of capital and the accumulated loss rising to €3 billion, i.e. more than a quarter of their total capital at end-2009. The private companies account for a smaller share of production but the bulk of foreign trade. Around 75% of Serbia's export is undertaken by companies in predominantly foreign ownership. Small and medium-sized enterprises contribute for just over 51% of the total value-added and slightly more than 57% of the overall employment. The informal sector, fuelled by weaknesses in tax and expenditure policies, as well as in law enforcement, including the fight against corruption and organised crime, remains large. It reduces the tax base and the efficiency of economic policies. *Overall*, structural adjustment of the economy has been lagging on the back of the slow reform process, which has been hampered by the economic crisis. The informal sector remains an important challenge.

State influence on competitiveness

State subsidies were relatively high at around 2.2% of GDP in 2009 following a nominal increase of almost a quarter compared to 2008. The amount of subsidies could be underreported as the state schemes as well as the individual state aid are not systematically referred for prior approval. The legislation on state aid control from July 2009 needs to be effectively enforced by the recently established State aid authority, but an appropriate monitoring mechanism is still missing. The state-controlled monopolistic structures remain in place. *Overall*, the state continues to influence substantially on competitiveness through its legal and financial mechanisms.

Economic integration with the EU

The EU has remained Serbia's main trading partner, accounting for 58% of the country's total exports and 57% of the total imports. The negative trade gap which Serbia had with the EU was declining steadily in the period to August 2010. Serbia also continued to improve a trade surplus with the countries in the region. The CEFTA countries account for 16% of Serbia's trade.

Export price competitiveness improved in 2009. Real gross wage growth at 0.2% was considerably smaller than average labour productivity growth, which translated into a 3% fall in real unit labour costs. In real effective terms, the dinar lost 3% of its value, despite consumer prices growing faster on the domestic market than abroad on average. In the first half of 2010, the real effective exchange rate of the dinar weakened further by some 7%. Against the background of subdued wage growth and increasing unemployment, unit labour costs continued to drop in real terms. *Overall*, trade integration with the EU remained high and export competitiveness continued to improve.

4. EUROPEAN STANDARDS

This section examines Serbia's capacity gradually to approximate its legislation and policies to the *acquis* related to the internal market, sectoral policies and justice, freedom and security, in line with the Stabilisation and Association Agreement and the

European Partnership priorities. It also analyses Serbia's administrative capacity. In each sector, the Commission's assessment covers progress achieved during the reporting period, and summarises the country's overall level of preparations.

4.1. Internal market

4.1.1. Free movement of goods

Progress can be reported in the field of the free movement of goods.

Legislation aligning with the New Approach Directives on safety of machinery, electromagnetic compatibility and low voltage equipment was adopted. The Ministry of Economic Affairs and Regional Development continued to play a central role in coordinating the establishment and improvement of the horizontal legislation, the quality infrastructure institutions and the transposition of the *acquis* on free movement of goods. Its capacity in this area has been strengthened with additional human resources.

Cooperation between the ministry and the Serbian Standardisation Institute, the Serbian Accreditation Board and the Directorate for Measures and Precious Metals has further improved.

As regards standardisation, the change of status of the Serbian Standardisation Institute (ISS) from an independent non-profit organisation to a public institution came into force in January 2010. During the reporting period the ISS further increased the number of adopted European standards (ENs), to a total of 8.986. The ISS is no longer responsible for type approval of vehicles, as the Traffic Safety Agency developed the capacity to take over this task. However, the chairman and members of the supervisory board have not yet been appointed.

In the area of conformity assessment and accreditation, the number of accredited conformity assessment bodies (CABs) rose to 413. Implementing legislation to the law on technical requirements for products and conformity assessment of products has been adopted.

There has been good progress on accreditation. The Law on Accreditation, fully aligned with the new legislative framework (765/2008), was adopted. The Serbian Accreditation Board extended the scope of its activities. It continued to provide training and seminars for assessors and its own staff and carried out awareness-raising activities. However, the chairman and the members of the supervisory board have not yet been appointed. The administrative capacity of the Board needs to be strengthened.

In the area of metrology, progress was made with the adoption of the new law in May 2010 and implementing legislation. The Directorate for Measures and Precious Metals has been restructured to implement the new law, and the government appointed the Metrological Council. The Directorate has been participating in the activities of international and European metrology organisations. However, further efforts are needed to continue aligning with the *acquis*, notably by implementing the already existing legislation and improving the limited capacity of the Directorate.

There has been progress on market surveillance. Implementing legislation in the area of general product safety and the Market Surveillance Strategy for the period 2010-2014 was adopted. The rapid exchange system providing information on dangerous products similar to RAPEX, NEPRO, was established. However, new legislation in this area, fully implementing the 2008 horizontal *acquis* on marketing of

harmonised products, remains to be adopted. The capacity of the market inspectorate needs to be strengthened, not least through training. Coordination between the different market surveillance authorities needs to be established, including the development of a common database.

There has been good progress in the field of consumer protection. The Law on Consumer Protection was adopted, transposing 14 relevant EU directives. A Consumer Protection Centre was established within the Ministry of Trade and Services aimed at solving the complaints brought by consumers, notably on contract warranty. Further steps have been taken towards establishing regional advisory centres for consumer protection which are to be devolved to non-governmental organisations. Training activities for professional staff have continued. The administrative capacity of the consumer protection department within the ministry has been improved, but the level of human resources remains insufficient. Public awareness-raising activities have increased. Consumer protection organisations have started improving their coordination.

The Law on Electronic Trade is in place. However, capacities for monitoring its implementation need to be further developed. The role of the ministry's Council for Consumer Protection remains limited. Consumer organisations are still weak and lack adequate resources. This continues to hamper their overall effectiveness. Public awareness-raising activities need to be further developed.

Overall, Serbia is moderately advanced on free movement of goods in meeting the requirements of the SAA in this area. A new legal framework for market surveillance still needs to be adopted. The administrative capacity and cooperation between the Ministries and other State institutions need to be further strengthened. Further efforts are required to continue transposition of the product-specific *acquis* into Serbian legislation.

4.1.2. Movement of persons, services and right of establishment

There has been little progress on movement of persons. With regard to the *coordination of social security* schemes, agreements on social insurance with Cyprus and Turkey were ratified. The Agreement on social security with Bosnia and Herzegovina was amended to further regulate the pension issues between the two countries.

Little progress was achieved in the provision of services. Preparations for transposing the Services Directive are at an early stage.

There has been little progress on *financial services*. Serbia prepared a roadmap for implementation of the Basel II framework. However, new legislation on banking, securities and insurance needs to be adopted. Serbia needs to further align with the Financial Services Directives. Serbia has yet to sign memoranda of understanding with all home supervisory authorities of foreign banks operating on its territory.

The National Bank of Serbia is responsible for supervision of the banking, insurance and voluntary pension fund sectors and is actively using its supervisory powers. The Securities Commission, responsible for supervising the capital market, is not sufficiently independent and does not operate fully in line with international standards. The supervisory capacity, in particular regarding employment and staff training, needs to be further strengthened to comply with the Capital Requirements Directive and requirements for risk-based supervision.

There was progress in the area of *postal services*. The law on postal services was further brought into line with the *acquis*. The parliament appointed the members of the Agency for Postal Services Council. It became operational as an independent regulatory body for postal services and the government adopted its financial plan. However, the administrative capacity in this area needs to be strengthened.

No progress has been made in the area of the right of establishment. As regards the recognition of professional qualifications and recognition of foreign degrees further efforts are needed.

Little progress has been made on company law. The One-Stop-Shop system is in its second phase and has shortened the time to set up a business to two days. Companies can submit an application for registration electronically. However, the e-Registration system has yet to become fully operational. The Company Registration Law and Securities Law need to be amended.

Some progress was made in the field of *accounting and auditing*. Amendments to the Accounting and Auditing Law, which are further aligned with the EU Accounting directives, were adopted. These amendments brought the statutory register and register of financial reporting to a single institution, the Business Registry Agency. However, strategy and action plan on upgrading corporate financial reporting remain to be fully aligned with the *acquis*.

Overall, preparations in the area of movement of persons, services and right of establishment are moderately advanced. A number of legal acts still need to be adopted.

4.1.3. Free movement of capital

Little progress was made on free movement of capital.

Serbian legislation provides for the free movement of credit related to commercial transactions or to the provision of services as well as to financial loans and credit with maturity longer than a year. While simplifying procedures for foreign payments, Serbia retains restrictions on short-term capital movements. Under the current law on foreign exchange, non-residents are free to make direct investments with restrictions in the arms sector and in some other areas laid down by the law. Under the law, foreigners may acquire real estate, subject to reciprocity, with the exception of agricultural land. EU investors are still having problems, due to the unclear legal status of the acquired real estate and incomplete process of property restitution, along with the very large number of permits required and the numerous granting agencies and authorities involved in the process. The implementation of the legislation on urban planning and construction remains slow.

Overall, Serbia is still moderately advanced in the area of capital movements. With certain restrictions, non-residents are free to make direct investments. Serbia needs to continue its efforts to meet the gradual liberalisation requirements laid down in the SAA.

4.1.4. Customs and taxation

Serbia has made good progress in the area of customs. The new Customs Law has been adopted and is largely harmonised with the *acquis*. The amended customs tariff nomenclature is fully in line with the 2010 EU Combined Nomenclature.

The Government adopted in September 2010 the Amendments to the Decree on Harmonised Custom Tariff Nomenclature for 2010. The amended decree has allowed Serbia to catch up with the liberalisation schedule for processed agricultural products (PAPs) and fishery products foreseen for 2010 in the Interim Agreement.

The administrative capacity of the Serbian customs administration has been further strengthened, notably by improved post-clearance controls and by the roll-out of an upgraded risk analysis system. Progress was also made through the conclusion of several agreements on international cooperation, where the customs also improved information sharing with other national institutions. In terms of trade facilitation, the customs administration formalised procedures for exchange of pre-arrival information with neighbouring countries.

Implementation of the integrated border management strategy and action plan continued. Serbia obtained the status of informal observer under the Customs Transit Convention. The country also participated in regular activities under the Customs 2013 Programme. Fight against corruption in customs was stepped up, which resulted in a higher number of disciplinary procedures based on internal controls. Two new free zones and one new customs house were opened. However, the IT infrastructure needs upgrading, in particular since the customs central IT system is reaching the limits of its capacity. The strategic planning process, both with regard to business and IT, should be reinforced.

Overall, Serbia is already well on the way to meeting the EU *acquis* and remains committed to reforms in the area of customs. The obligations stemming from the Interim Agreement were well respected. Further efforts are needed as regards legislative alignment, and administrative capacity, including preparing for IT interconnectivity and interoperability with EU IT systems.

In the area of taxation, some progress has been registered. The parliament adopted amendments to the law on company profits tax and the law on income tax, in line with the EU *acquis*. In July, the Serbian Parliament adopted amendments to the Law on Tax Procedures and Tax Administration. Implementing legislation by which the Large Taxpayer Centre will cover larger number of tax payers was adopted in July which should result in higher collection of revenues. Implementing legislation on tax identification number of legal entities aimed at simplifying procedure and cutting unnecessary paperwork in line with the comprehensive regulatory reform was also adopted in July. Laws on avoidance of double taxation were ratified for a number of EU Member States. However, discriminatory excise duties on imported spirits need to be brought into line with the same duties on local production in order to comply with the relevant provision of the Interim Agreement.

The administrative capacity of the Serbian tax administration continued to improve as a result of intensive training efforts. In April 2010 the administration opened a new Contact Centre as an integrated and centralised information point for taxpayers. Some new organisational units, such as groups for strategy and coordination, for risk management and for internal audit, were created in December 2009. New management tools were developed and the overall business strategy was adopted in June 2010. At the end of 2009 a single taxpayers' register was completed, as the basis for the future new information system. However, despite good results in enforcement by the tax police, the general collection capacity of the administration improved only slightly. The share of the 'grey' economy remains high and cumbersome procedures for tax collection remain in place.

Overall, in the area of taxation, Serbia is well on the way to meeting the EU standards. The enforcement capacity of the tax administration and tax collection has improved, although further progress is required in this respect. In addition, the problem of the informal economy remains yet to be tackled. Serbia needs to take follow-up action to ensure that its tax legislation complies with the Code of Conduct for business taxation.

4.1.5. Competition

Some progress can be reported in the area of anti-trust.

Implementing legislation pursuant to the law on competition protection was adopted, further aligning Serbia with the Interim Agreement (IA) requirements. This covers notably market definition, merger notifications, individual and block exemptions for restrictive agreements fines and leniency program. The Commission for the Protection of Competition (CPC) has continued its activity and has adopted decisions on mergers and abuse of dominant positions further improving its track record. It has also adopted guidelines for implementing legislation. The services of the Commission for the Protection of Competition were restructured, notably by establishing separate divisions for economic analysis and legal affairs. The CPC's capacity to carry out economic analysis has been strengthened. A number of cooperation agreements were signed with sector-specific regulators as well as with competition authorities of some EU Member States and neighbouring countries. The president and members of the Council of the Commission for the Protection of Competition were elected by the Serbian Parliament in October 2010.

However, the law on competition protection has been undermined by the adoption of some conflicting horizontal legislation notably on mandatory car insurance. The financial plan of the CPC for 2010 has not yet been adopted by the Government. The CPC's capacity to carry out economic analysis and to deal with procedural matters remains to be further strengthened in order to fully implement with the IA requirements. Moreover, the CPC needs to improve its expertise and knowledge in procedural matters. The capacity of the judiciary to deal with substantive issues of competition remains weak and significant efforts are needed in this respect. A solid enforcement record remains to be demonstrated.

There has been some progress in the area of state aid. A State aid authority was established in December 2009, as required by the SAA, and became operational in April 2010. The Commission is supported by the Permanent Secretariat of the State Aid Control as an independent department within the Finance Ministry. In July 2010 the Commission for State Aid Control adopted the State aid inventory for 2009. However, the administrative capacity of the State aid authority secretariat needs to be substantially strengthened. Serbia needs to continue its efforts to establish a track record in enforcing State aid decisions.

Overall, Serbia remains moderately advanced in meeting the Interim Agreement requirements in the area of competition. However, the capacity and the expertise of the Commission for the Protection of Competition and of the judiciary have to be strengthened.

4.1.6. Public procurement

Little progress has been made in the area of public procurement. The Public Procurement Office (PPO) published a number of decision templates and models of

tendering documentation, with the aim of assisting the contracting authorities. The PPO carried out training seminars for various stakeholders throughout the country and further promoted and serviced the public procurement web portal. The members of the Commission for the Protection of Bidders' Rights were appointed in October 2010.

However, the substantial delays in the establishment of the new Commission for the Protection of Bidders' Rights have undermined the overall development of the public procurement framework. In addition, shortcomings in the existing legislative framework, including the lack of an appropriate regulatory framework on concessions, still remain to be addressed. The weak administrative capacity of public procurement bodies, in particular the public procurement unit in the Ministry of Finance, the PPO and the review body, has persisted. The financial resources of these bodies remain scarce. The coordination mechanisms among the main stakeholders in the public procurement system, especially with a view to reducing the scope for corruption, remain weak. The certification of public procurement officials has not yet started. The strategy for upgrading the public procurement system in Serbia remains at early stage. As a result, inefficiencies in the use of public money persist, as detected by the Supreme Audit Institution in its 2008 budget audit report.

Overall, Serbia's preparations for establishing an effective and fully independent public procurement system with streamlined award procedures are still moderately advanced. Significant efforts remain necessary to strengthen the capacity to implement the EU *acquis* in this field.

4.1.7. Intellectual property law

Progress has been made in the area of intellectual property rights. The Intellectual Property Office (IPO), which plays the role of national coordinator for intellectual property rights, has set up an in-house education and information centre. However, the financial sustainability of the IPO has been a source of concern. Discussions on the long term financial sustainability of the IPO have been ongoing but no solution has yet been found. The national intellectual property rights strategy needs to be finalised.

A new law on copyright and related rights was adopted in December 2009 and was followed by implementing legislation. It establishes a Commission on Copyright and Related Rights empowered to decide on the tariffs if no agreement is reached between the associations for collective management of copyrights. However, the members of the Commission have not yet been appointed by the Government. The law on optical discs remains to be adopted.

Progress was made in relation to industrial property rights. As of October 2010, Serbia has become member of the European Patent Organisation. In line with the Interim Agreement, some international conventions including the European Patent Convention as well as the International Union for the Protection of New Varieties of Plants Convention were ratified. Legislation on industrial design, on topography of integrated circuits and on indications of geographical origin has been adopted, in line with the Interim Agreement. The new law on trademarks introduces an administrative procedure for appealing against IPO decisions. A newly adopted Strategy for Scientific and Technological Development fosters a number of innovative activities, and provides an indirect impetus to raise the number of patent applications. However, the law on patents has not yet been adopted.

Some progress was made in the field of enforcement. Serbia has set up specialised units (high-tech crime prosecutor, police cyber unit, specialised customs unit, tax unit and tax police) aimed at enforcing the legislation in this area. The length of investigations has been shortened. The frequency of checks by tax inspectors has risen, whereas the number of cases brought for prosecution has dropped, pointing to better compliance overall with the law. Seizures by market inspectors have further improved. The customs administration has continued to make progress in enforcing intellectual property rights. It fully updated an electronic database of customs offences in the field of intellectual property rights and introduced electronic handling of requests for protection of Intellectual Property Rights. A Memorandum of Understanding has been signed between the Intellectual Property Office and the Judicial Academy to provide specialised training.

However, specialisation of judges and court panels in this area needs to be ensured. Inadequate storage space for counterfeited and pirated goods that infringe copyright and related rights or other industrial property rights continues to be a problem.

Overall, Serbia's preparations in the area of intellectual property law remain moderately advanced. Further efforts are needed in terms of alignment with the *acquis*. Concerning enforcement, better co-ordination among relevant agencies is required, as well as substantial investment in specialised judicial training.

4.1.8. Employment and social policies, public health policy

Some progress has been made on employment policy. Implementing legislation concerning the law on employment and unemployment insurance and the law on vocational rehabilitation and employment of disabled persons was adopted. In September 2009 the action plan for implementation of the youth employment policy for 2009-2011 entered into force. In February 2010, the government adopted the national action plan for employment for 2010, which defines priorities, goals, programmes and measures of employment policy. The plan is the main instrument of an active employment policy aimed at boosting investment in human resources, supporting social inclusion in the labour market and creating new jobs. In August 2010, the national employment action plan for 2011 was adopted to provide continuity in implementation of the employment strategy. The general budget cuts in response to the economic crisis did not affect the budget allocated to active labour market policies. The government also continued with start-up loans aimed at generating new jobs.

The national employment service has reallocated its human resources to keep administrative capacity unchanged for its main functions. A centre for professional rehabilitation and employment of disabled persons has been established, as well as a Fund for employment of young persons. From January until September 2010 the number of employed persons with disabilities increased. Coordination and cooperation between the ministry and the national employment service has improved and regular monthly meetings have been established. The Republican Health Insurance Fund has completed a database on all insurers, and established a system for social security registration with the national employment service, thus simplifying the registration procedure.

All these measures have been used to counter the impact of the economic crisis and maintain the level of employment but have not brought the desired results. Only a limited share of unemployed people could be addressed, whilst in the aftermath of the

global financial and economic crisis unemployment continued to rise and the employment rate dropped to 50%. The situation of young jobseekers and of long-term unemployed is of particular concern. The economy continues to suffer from skills mismatch. Serbia has to face considerable labour market challenges and the policy response is insufficient to deal with the scale of the problem.

Regarding social policies, there have been no changes to the Labour Law since the amendments made in July 2009.

Some progress has been made in the area of *health and safety at work*. Activities related to implementation of integrated inspection control have intensified. Under this approach, one inspector will be competent to carry out inspection of workplaces concerning compliance with both the labour law and occupational health and safety regulations. In the legislative area, several Rulebooks were adopted with the aim of transposing EU Directives on health and safety at work into national law. A rulebook on risk assessment was amended. The Occupational Safety and Health Strategy Action Plan were adopted. An action plan for 2010-2014 for the labour inspectorate has been drawn up. However, despite an improvement, the number of accidents at work remains high.

As regards *social dialogue*, amendments to the law on peaceful settlement of work disputes were adopted. This enlarged the list of disputes that can be treated under this law and prescribed conditions for appointing an arbitrator. The amended law regulating the work of the Agency for Peaceful Settlement of Labour Disputes was passed by parliament. However, social dialogue is weakened by the unresolved issue of representativeness of the social partners and a burden of mistrust among the social partners. Moreover, the input of social partners into the decision-making process and the drafting of legislation remains limited due to both the government's lack of strategic approach in the consultation process and to the limited capacities of the social partners. The functioning of the Economic and Social Council at central as well as at municipal levels still needs to be improved. Bipartite social dialogue is still rather weak.

Regarding *social inclusion*, after having established the team for social inclusion in 2009, the government continued with establishment in early 2010 of the working group on social inclusion, made up of representatives from all institutions in charge of defining, implementing and monitoring social inclusion. However, with the economic crisis, poverty has risen: the rate of those living below the absolute poverty level rose from 6.1% in 2008 to 6.9% in 2009, while the rate of those living below the relative poverty level rose from 13.2% in 2008 to 13.6% in 2009. As the number of those living close to this relative poverty level is quite high, further deterioration of the economic situation may increase these rates. Fighting poverty and social exclusion, not least of vulnerable categories of the population, with particular reference to the Roma population, Roma refugees, IDPs and some pensioners, remains a key challenge. The deepening disparity between regions is a matter of concern.

Concerning *discrimination*, an important step forward was appointment of the Anti-Discrimination Commissioner in early 2010. The Commissioner has a wide range of duties related to dissemination of information on discrimination, providing legal support to the victims of discrimination and monitoring the implementation of laws which may have discriminatory elements, including the right to initiate amendments or new laws related to this topic. However, further efforts are needed to ensure that the Commissioner becomes operational. A comprehensive approach in the field of the anti-discrimination policies remains to be ensured. Vulnerable groups, such

as Roma, persons and children with disabilities and the LGBT population, remain the most exposed to discrimination.

As regards *gender equality*, the law on gender equality was adopted and has been in force from December 2009. In August 2010, the Government adopted an action plan for implementation of the national strategy aimed at improving position of women and gender equality. Harmonisation with EU legislation has also been carried out. Institutional structures have been established, and despite the general context of budget cuts and a staff freeze, the number of staff dealing with this policy was maintained. However, women and in particular disabled women, single mothers, older women and those living in rural areas still continue to face discrimination in the labour market. Women are under-represented in decision-making positions.

In the area of *social protection*, the amendments to the law on financial support to families with children were adopted in December 2009. In May 2010, the rulebook on the work of centres for social care was adopted. However, the pension system continues to record a high deficit despite pension reforms conducted in recent years. Many older people are exposed to poverty, including those not covered by the pension system.

There has been progress in the area of public health. The National Health Council of Serbia prepared the strategic 'Health Protection Development Plan' for 2010-2015, which is pending adoption by the Parliament. In the fields of *blood and tissues and cells*, the Directorate for Biomedicine was established within the Ministry of Health, and a coordinator for organ, tissue and cell transplantation has been designated at the Clinical Centre in Serbia. Furthermore, an awareness-raising campaign on transplantation has been launched. The legislation on biomedicine and transfusion is being implemented. Some progress can be reported in the field of *tobacco*. The law on protection from exposure to second-hand tobacco smoke has been adopted. However, pictorial health warnings remain to be introduced on cigarette packages.

The law on drugs and medical devices was adopted in April 2010. Activities related to *mental health, cancer prevention, communicable diseases and alcohol* continued. The Serbian Institute of Mental Health was designated as a WHO Collaborating Centre for mental health care and workforce development. Good cooperation with the European Centre for Disease Prevention and Control continues. However, efforts towards de-institutionalisation and community-based institutions need to continue. The administrative capacity of the Ministry of Health and of the Institute for Public Health needs to be strengthened. Further efforts are needed to implement adopted strategies.

Overall, preparations are continuing towards meeting European Standards in the areas of employment and social policy. However, declining employment rates and increasing unemployment are a source of concern, in particular with regard to young people and the most vulnerable groups.

4.1.9. Education and research

Some progress has been made in the field of education. Serbia has started reforms in primary and secondary levels of education and is continuing Bologna reforms in higher education. With the help of the European Training Fund, it is starting the process of reforming its vocational education and training system.

Several laws in the field of education and training were adopted in 2010. In April a new law on pre-school education aimed at improving the quality and access to

education was adopted. In May a Law on Pupils' and Students' Standards has been adopted, based on the principle of social inclusion. Amendments to the Law on Higher Education were adopted in June 2010 by the Parliament.

Primary and secondary school curricula have been revised and were implemented in September 2010 in the first year of secondary level. As regard higher education, the European Credit Transfer and Accumulation System (ECTS) has been fully implemented in all higher education institutions. The three-cycle system is in place and preparation of doctoral studies under Bologna guidelines is starting. In the vocational education and training (VET) sector, the Council for Vocational Education and Adult Education has been established; it is a tripartite body with key functions including links with business, national qualification framework and curricula.

Wide consultations with youth and social partners have been initiated with a view to developing a Youth Law. Another 12 Youth Offices have been opened as part of the strategy for quality leisure time and personal development of young people.

However, an overall strategy covering all levels of education, including lifelong learning, needs to be developed. A national qualification framework remains to be adopted. Adult education is weak and needs a reform of contents, methods and infrastructure. The process of accreditation of universities and programmes has not been completed. Adjusting the education system to the labour market needs further improvement. Planned investment in the education sector has been cut from 3.9% to 3.3% of GDP.

Good progress has been made in the field of culture. Serbia's participation in the EU's Culture Programme has been increasing steadily. The UNESCO Convention for the Safeguarding of the Intangible Cultural Heritage and the Council of Europe Framework Convention on the Value of Cultural Heritage for Society have been ratified.

Good progress was registered in the area of science and research. Serbian research entities have continued to successfully bid for research projects under the 7th EU Research Framework Programme (FP7). Serbia has improved its administrative capacity to implement the FP7 Memorandum of Understanding by appointing additional contact points and observers in the FP7 management committees. Interministerial cooperation has been strengthened in relation to Serbia's participation in the Competitiveness and Innovation Programme (CIP). Negotiations to associate Serbia with the 7th Euratom Research Framework Programme (2007-2011) are ongoing. In February 2010, Serbia and the Joint Research Centre (JRC) concluded a memorandum of understanding on scientific and technological cooperation which will provide additional research opportunities.

With respect to future integration into the European Research Area (ERA), Serbia adopted a national strategy for scientific and technological development 2010-2015 in February 2010 and has appointed observers in most ERA governance bodies. In March 2010, further legislation was adopted, particularly with respect to issues such as innovation, scientific and research activities and intellectual property rights. This addresses the brain drain and reforms the Serbian Academy of Sciences. In May 2010 a bill was adopted allocating €400 million to fund research at national level over the four coming years. However, both public and private investment in research remains low (less than 0.5% of GDP) and Serbia generally needs to reinforce its national research capacity.

Overall, Serbia is moderately advanced towards meeting European standards in the area of *education*. However, an overall strategy involving all levels of education, including lifelong learning, remains to be developed. The implementation of the recent reforms should be monitored closely. Further efforts are needed in the field of vocational education and training. Further efforts are needed to facilitate Serbia's integration into the European Research Area and to strengthen its national research capacity.

4.1.10. WTO issues

Negotiations for Serbia's accession to the World Trade Organisation (WTO) are nearing their end, the bilateral track of negotiations being already completed with most WTO partners. Progress has also been made on the multilateral track. However, finalisation of the process will depend on the pace of remaining bilateral negotiations and internal reforms. Serbia is well placed to meet its objective of joining the WTO.

4.2. Sectoral Policies

4.2.1. Industry and SMEs

Little progress was made in the SME sector.

Serbia continued previous efforts to move from the phase of policy formulation and the identification of strategic objectives to policy implementation in support of innovative companies, start-ups, provision of business services and information dissemination.

The action plan for 2009 was successfully implemented — with some activities however postponed due to lack of financial resources. The action plan for 2010 was adopted and is currently being implemented. The SME Business Council, with 80 SME representatives, was established in March 2010 and steps to link it up with other private initiatives have been taken. The transformation of the SME Agency into the National Agency for Regional Development has been finalised. Financial support continued with start-up loans, investments in underdeveloped areas, programmes for innovation and clusters.

Serbia continued its participation in the Entrepreneurship and Innovation Programme and joined the Information Communication Technologies policy Support Programme in 2010, thus becoming a member of two out of the three operational programmes under the EU's Competitiveness and Innovation Programme. Serbia also continued being active in the Enterprise Europe Network.

In the reporting period Serbia continued implementing several measures to improve SME's access to finance and more specifically the support of start-ups. However, developments in the area of SMEs were affected by the shift of the focus of the ministry in charge of SMEs to regional development and also by a significant cut in human resources in its SME department. Reduced administrative capacity raises concern for the implementation of the national strategy for SME development 2008–2013 and for the implementation of the Small Business Act. The level of cooperation between the ministry in charge of policy and the agency in charge of implementation needs to be improved.

Serbia has made little progress in developing and implementing a modern industrial policy. The industrial strategy remains to be adopted.

Overall, Serbia's preparations in the area of industry and SMEs are well advanced. However, reduced administrative capacity may adversely affect the good level that the SME policy has attained.

4.2.2. Agriculture and fisheries

Progress can be reported in the area of agriculture and rural development, food safety, veterinary and phytosanitary policy.

In the area of agriculture and rural development, legislation on farm advisory systems has been adopted. The Directorate for Agrarian Payments, which is planned to serve as a future Instrument for Pre-Accession Assistance for Rural Development (IPARD) agency, has been established. An action plan for IPARD programming and the establishment of the operating structures have been developed and a regular reporting mechanism on its implementation has been initiated. Two new regional rural centres have been established within the national rural development network, bringing their number to 16 country-wide.

However, implementation of the law on agriculture and rural development remains to be completed. The national strategy for agriculture and rural development, the national programme for agriculture and the national programme for rural development have not yet been adopted. The managing authority remains to be appointed. The Directorate for Agrarian Payments remains to be fully staffed. An interministerial mechanism for coordinating rural development policies has yet to be established.

Progress has been made in the wine sector. Implementing legislation for the vineyard register has been adopted. The University of Belgrade, Faculty of Agriculture, Department for Viticulture, has been appointed as the control organisation responsible for the 'System of Designation for Wine with Geographical Indication'. However, the vineyard register remains to be established. The procedure for the authorisation of the oenology laboratories has not started. Implementing legislation regulating import conditions and marketing and quality matters remains to be adopted.

Some progress has taken place on quality policy. The law on indications of geographical origin was adopted, further aligning with the EU *acquis* and reinforcing implementation of the requirements of the Interim Agreement on the protection of geographical indications registered in the Union.

Some progress has been made on organic farming. A National Action Plan for the development of organic farming has been adopted. A new law on organic farming was adopted with entry into force foreseen in 2011. It establishes the Directorate for National Reference Laboratories as the competent authority for organic farming. However, the Accreditation Body of Serbia needs to be internationally accredited in order to allow for the new law to enter into force in January 2011.

Little progress has taken place in the area of food safety. Implementing legislation relevant for allowing export to European Union was adopted. However, the implementation of the law on food safety needs to improve. Substantial implementing legislation needs to be enacted and enforced. The principle of risk analysis is not yet applied and an adequate database system needs to be set up for this purpose. The Hazard Analysis and Critical Control Points Plans need to be better implemented by operators and associated official controls. Inspections and controls at the external

border need to be further upgraded. The ministry needs to improve capacities to take on its new competences on food safety.

Little progress can be reported as regards upgrading of agri-food establishments. The instruction on hygiene requirements and official controls of products and establishments being approved for exports of milk and dairy products and exports of fish and fishery products to the EU was adopted following the Food and Veterinary Office mission's recommendations. However, a national programme for upgrading the establishments remains to be adopted.

Progress has been made in the veterinary area. The amendments to the law on veterinary matters were adopted. They further align the legislation with the EU *acquis* on border issues and simplify the current system of import licences. The law on medicine was adopted, establishing limits on residue levels. Implementing legislation was adopted among other things on conducting border veterinary controls, eradication of a number of diseases and animal welfare. In the field of animal welfare, two European conventions on pets and protection of vertebrate animals were ratified.

However, further amendments to the import licensing system will be necessary as the current system is not compatible with the *acquis*. The implementing legislation on border controls is not enforced and veterinary inspections and controls at external borders have not been upgraded. Enforcement of legislation in relation to registration and control of all cattle markets needs to be improved. Awareness of the legal framework for animal identification and registration needs to be raised and IT infrastructure needs to be upgraded. The Veterinary Directorate's capacities for database operation need to be strengthened. The Veterinary Inspectors need continuous training on the new principles introduced by legislation.

Progress has been made concerning official control laboratories. The Directorate for National Reference Laboratories has been established and is partly operational. The legal competence of the National Reference Laboratories has been extended to animal health. However, the administrative capacity of the Directorate remains to be further improved. The national reference laboratories are not operational. The administrative competence with regard to seeds needs to be clarified. The funding and charging policy for laboratory tests at the border is not unified.

As regards genetically modified organisms (GMOs), the law banning imports of genetically modified reproductive material needs to be amended to be aligned with the *acquis* and WTO requirements.

Some progress has taken place in the phytosanitary area. The law on recognition of plant varieties was adopted. The International Convention for the Protection of new Varieties of Plants was ratified. Implementing legislation has been adopted on control of potato bacterial diseases. Implementing legislation for the law on plant nutrition products and for the Law on Plant Health has been adopted. A rulebook on maximum residue levels of plant protection products in food has been published. Implementing legislation has been adopted in the area of plant breeders' rights. However, further implementing legislation needs to be adopted especially for the Law on Plant Protection Products. The procedure for registration of new plant protection products is not harmonised with the EU *acquis*. There is no official pesticide residues monitoring programme meeting the EU requirements in place. The strategy and action plan for the introduction of a plant passport scheme are not yet adopted. Control at external borders has not been upgraded.

Progress has taken place in the area of fisheries. Implementation of the new legal framework has almost been completed. The distribution of competences between the ministries has been clarified. Serbia has been included in the list of countries allowed to export fishery products to the EU.

Overall, Serbia is advancing well in the areas of agriculture and rural development, food safety, veterinary and phytosanitary policy towards meeting European Standards. The legal framework continues to improve. However, implementation and enforcement of the legislation need to be upgraded, especially in the food safety area. Administrative capacity is weak and needs to be more efficiently allocated. Inspection services need further training. Recruitment of qualified staff needs to take place in the newly established bodies.

4.2.3. *Environment*

Good progress can be reported in the area of the environment.

As regards horizontal legislation the National Programme for Environmental Protection (NPEP) 2010–2019 was adopted. The financing projections outlined in the NPEP are based on a low-cost scenario and on increased user charges, which will require considerable liberalisation of current tariff policies. The Serbian Environmental Protection Agency continues to maintain a good level of cooperation with the European Environment Agency.

In the area of air quality, progress can be reported. Implementing legislation to the law on air quality was adopted. However, implementing legislation on emission limit values and emission measurements at large point sources remains to be adopted.

Progress can be reported on waste management. A regulation on establishing the plan for the reduction of packaging waste for the period from 2010 until 2014 has been adopted, following the adoption of laws on waste management. In addition, the National Waste Management Strategy (NWMS) was adopted. The NWMS provides guidance on the implementation of waste legislation. It establishes systems for the management of specific waste streams. However, the procedures for setting product charges, as well as criteria and procedures for the Environmental Fund to finance waste recovery and recycling activities need to be further established. Waste management plans at regional and local levels have to be developed.

There has been progress on water quality. A new law on water was adopted. Water management is to be financed by the national and the Vojvodina provincial budget, as well as by water fees, concession fees and other funds. Dissuasive water pollution fees are to be paid to the Environmental Protection Fund and to be used for the construction of waste water treatment plants. However, there is still no system to monitor nitrate concentrations in and contamination of groundwater. The wastewater treatment infrastructure throughout the country needs upgrading. The Water Directorate within the Ministry of Agriculture, Forestry and Water Management remains to be strengthened. The administrative capacity of the water directorate was reduced.

Progress can be reported on nature protection. Serbia adopted the law on wild game and hunting in March 2010, aligning further with the *acquis* and international obligations under the Bonn Convention on Conservation of Migratory Species of Wild Animals. Serbia adopted the new law on forests, which provides for a framework to protect the forest against atmospheric pollution and fire. However, the strategy on biodiversity remains to be adopted.

On industrial pollution control and risk management there has been some progress. The process of implementing the International Plant Protection Convention has started with the first applications received from existing installations in the cement industry as well as from a new installation for pesticide production. The list of installations which will have to comply with the *acquis* before 2015 is being revised.

Good progress can be reported on chemicals. The Chemicals Agency, a regulatory and implementation body dealing with biocidal products and chemicals became operational.

Concerning climate change, good progress can be reported even if a number of important implementation steps remain. The National Strategy for Incorporation of Serbia into the Clean Development Mechanism under the Kyoto Protocol was adopted by the Government in February 2010 for agriculture, forestry and waste management sectors. The first National Communication under the UNFCCC and greenhouse gas inventory is under development and is expected to be finalised in 2010. Serbia also associated itself with the Copenhagen Accord. A national ozone office was established within the Ministry of Environment and Spatial Planning responsible for the phasing out of ozone depleting substances. There has been an improvement in human resources working on climate change but further increase in staff is still needed.

As regards noise, there has been no progress in implementation of the legislation.

As regards administrative capacity there was little progress. Further training was provided to the environmental protection inspectorates. The Environmental Protection Agency remains fully operational and its performance is improving. The Environmental Protection Fund continues to be active. However, it still lacks the capacity to ensure proper implementation of the integrated monitoring strategy. Budgetary resources for environmental protection remain low. The institutional capacity needs to be strengthened, especially at local level. Better coordination with the central level as well as further enforcement remain necessary.

Overall, Serbia is moderately advanced in the area of environmental protection towards fulfilling the European standards. The capacity to implement and enforce legislation remains to be strengthened.

4.2.4. Transport policy

Serbia has made some progress in the area of transport.

In the area of trans-European transport networks, there has been some progress. Serbia participated in the update of the Multiannual Plan 2010-2014 of the South East Europe Transport Observatory (SEETO). A new road route was introduced in the Core Network within Serbia. A General Master Plan covering infrastructure projects for all modes of transport up to 2027 was adopted. The action plan for 2010 for the implementation of the national transport strategy was adopted. Regarding the implementation of the action plan for construction of Corridor X, works on some road sections have continued. However, the implementation of the action plan is at an early stage, with the company responsible for Corridor X being restructured.

There has been some progress in the area of road transport. Serbia has allowed unrestricted transit traffic for EU carriers to comply with its obligation under the Interim Agreement. The European Agreement concerning the International Carriage of Dangerous Goods by Road has been ratified. The agreement with Montenegro on transport of passengers and goods in international road transport was ratified. The law

on road safety entered into force in December 2009. The number of road accidents has been reduced over the reporting period. The amendments to the law on international road transport have further aligned national legislation with the *acquis* by introducing the certificate of professional competence for managers. Implementing legislation on driving and rest periods, digital tachographs and technical conditions of vehicles has been adopted. The Agency for Road Safety has been established and became operational in September 2010.

However the legislation on transport of dangerous goods, on transport of passengers and on carriage of goods remains to be adopted. An interministerial coordination body needs to be established for road safety and the implementing legislation needs to be adopted. The implementation of digital tachographs has been delayed due to the lack of administrative capacity.

In rail transport, there has been little progress. Regarding restructuring of the railway sector, the methodologies for determining the public service obligation and for calculating access charges for railway infrastructure were adopted. Implementing legislation on the public service obligations and compensations has been adopted. Serbia has ratified the Bilateral Agreement with Montenegro for border control in railway traffic.. However the conditions for full market opening are not in place to allow gradual market opening. The law on railways has not yet been amended. No Network Statement has yet been published. The separation of accounts between infrastructure and services within the infrastructure manager has not yet taken place. The Directorate for Railways is still not exercising its role as regulatory body.

Little progress has taken place in combined transport. Serbia has ratified the Agreement with Hungary on combined transport and logistical services and the agreement has started to be implemented.

Good progress was made in inland waterways. Serbia has adopted six international conventions of the International Maritime Organisation. Serbia has also ratified the bilateral agreement with Croatia on navigation on inland waterways and their technical maintenance. The Law on Navigation and Ports on Inland Waterways has been adopted. However, river information systems need to be set up.

Good progress has taken place in air transport. The provisions of the European Common Aviation Area (ECAA) Agreement in relation to market access have been applied and the market has been opened to new carriers. The law on civil aviation aimed at implementing the first transitional phase of the ECAA has been adopted, addressing a number of previously outstanding issues in the field of aviation safety, ground handling, and aviation security. On air traffic management, Serbia organised with Montenegro their respective airspace into a functional airspace block. However, Serbia still needs to make further efforts to complete regulatory alignment with the single European sky within the Implementation of Single European Sky in South-East Europe (ISIS) Programme. Legislation of the single European sky, in particular the regulations on provision of air navigation services, organisation and use of airspace, interoperability of the European Air Traffic Management network and the flexible use of airspace regulation need to be adopted. Separation of responsibilities for inspection and audits as well as establishment of an independent air accident investigation has not yet been done. The security control system remains to be overseen by an independent body. The administrative capacity of the ministry has not been reinforced.

Overall, Serbia is moderately advanced in the area of transport. It has continued to comply with the obligations of the Interim Agreement and SAA. Market access provisions of the ECAA Agreement are now applied. Framework legislation has been adopted for inland waterways and air transport. However, framework legislation remains to be adopted for railways. Reform of the railway sector needs to be stepped up. Administrative capacity needs to be strengthened for the implementation of the adopted legislation.

4.2.5. Energy

Some progress can be reported in the energy sector. The programme for implementing the current Energy Sector Development Strategy 2007-2012 was revised in April 2010.

There has been little progress in security of supply, with no developments as regards oil stocks. At an estimated 45 days, they remain far below European requirements (90 days), and oil stocks legislation remains to be adopted. There has been an increase in gas reserves. Construction of the underground gas storage facility in Banatski Dvor has been completed with a view to securing gas supplies in the event of unexpected cuts from current sources. A joint venture for the storage facility was established with Gazprom (51%) in October 2009. The contract for the establishment of a joint company for the construction of the South Stream gas pipeline through Serbia was signed in October 2009. In March 2010 a Joint Statement for the development of the Nis-Dimitrovgrad gas interconnector with Bulgaria was signed.

However, the financing of the project needs to be secured. Natural gas interconnections between Serbia and other countries in the region remain limited and there is no physical possibility for diversification of gas supply sources.

As regards electricity interconnections, the 400 KV overhead lines between Nis and Leskovac have been completed. The section from Leskovac to the border with the Former Yugoslav Republic of Macedonia is still under construction as well as the new line with Romania. As a result of the agreement on cooperation in the energy sector with Russia, a contract was signed for the sale of the Serbian oil company NIS to the Russian Gazprom Neft. However, following a complaint from the Kosovan Transmission System Operator, the Secretariat of the Energy Community launched a dispute settlement procedure taking the preliminary view that Serbia “failed to fulfil its obligation under the Energy Community Treaty”.

Serbia made little progress in the context of the internal energy market. In the electricity sector, transmission costs have been separated from other costs. The electricity transmission system operator has, to a large extent, become financially sustainable. Formal opening-up of the electricity and gas markets to non-household consumers has been completed. The Energy Regulatory Agency (AERS) has been working well, in line with Energy Community Treaty requirements.

However, several competencies foreseen under the Energy Community Treaty have not been granted to the regulator. Tariffs are not yet cost-reflective. Amendments to the Energy Law, concerning the supply function in both the electricity and gas sectors and extension of the legal responsibilities of the AERS, remain to be adopted. The separation of distribution and supply in the electricity sector still has to be completed. The deadlines set by the Energy Treaty have not been met. Further efforts are needed to achieve unbundling and real market opening together with a pricing

policy offering a sustainable tariff reflecting costs. In the gas sector, the legal unbundling of Srbijagas remains to be achieved along with proper implementation of the Regulation on conditions for access to the natural gas transmission networks.

There has been little progress in energy efficiency and renewable energy. The national energy efficiency action plan was adopted in July 2010. The government adopted implementing legislation on renewable energy in November 2009, namely on privileged producers of electricity, including incentive measures (feed-in tariffs) for electricity produced from renewable energy sources. However the main elements of the *acquis* on renewable energy remain to be transposed. Serbia does not have a legislative framework on energy efficiency in place. The law on rational use of energy remains to be adopted.

Serbia has made some progress in the areas of nuclear safety and radiation protection especially concerning the decommissioning programme of the “RA” research reactor at Vinca. Decommissioning of the Vinča research reactor, preparation for the repatriation of spent nuclear fuel to the Russian Federation and management of radioactive waste on-site are progressing well although not fully in line with the planned time schedule. The Serbian Radiation Protection and Nuclear Safety Agency (SRPNA) were established in December 2009 and became operational in the second half of 2010. The Director of the Agency was appointed in July 2010.

However, legislation and working procedures in the nuclear area need be revised in order to comply with the EU *acquis*. Working procedures, appropriate staffing and technical means have to be established to enable the SRPNA to work properly. Responsibility for inspection and the operating budget for the Agency need to be clearly defined. Serbia still needs to ratify the Convention on Nuclear Safety and the Joint Convention on the Safety of Spent Fuel Management and on the Safety of Radioactive Waste Management.

Overall, Serbia is moderately advanced in the implementation of the SAA and of the European standards in the energy sector. Further efforts are needed to achieve unbundling and real market opening together with a pricing policy offering a sustainable tariff reflecting costs. The implementation of the internal market requires transparency and non-discriminatory access rules. To this end, the current Energy Law needs to be amended and put in line with the electricity and gas *acquis*, and the role and independence of the AERS needs to be strengthened. Further efforts need to be made to strengthen the nuclear regulator.

4.2.6. Information society and media

Some progress can be reported on electronic communications and information technologies. The law on electronic communications was adopted by the parliament in June 2010. The law aims at approximating the Serbian legislation to the 2002 and partly the 2009 EU regulatory framework on electronic communications. The new strategy for electronic communications was adopted in September 2010. The Regulatory Agency has adopted rules on costs for radio station licence issuance and on radio frequency usage fees. It has also adopted a decision on designation of universal service operators and adopted rules on number portability in public mobile telecommunication networks which will enter into force in 2011. However, few competitive safeguards have yet been introduced and tariffs are not rebalanced. Market competitiveness is still limited.

The process of privatising the incumbent operator in the fixed telephony market has been launched. In February 2010 a second national fixed telephony licence was awarded for an initial period of 10 years but with the agreement not to allow similar new licences until the end of 2011, thereby keeping competition in the sector limited despite the adoption of the primary law.

Concerning administrative capacity, both the Regulatory Agency and the ministry need to be strengthened. In particular, the regulator needs expertise to ensure the implementation of the new law on electronic communications. The board members of the regulatory authority remain to be appointed.

There has been some progress on information society services. A law regulating e-commerce and implementing legislation regarding the law on electronic documents have been adopted. Concerning electronic signatures, two more certification service providers were certified. The government adopted in October 2009 the strategy for e-government development and the action plan for its implementation from 2009 to 2013 as well as the national broadband strategy and action plan. A 10 year strategy for development of the information society in Serbia was adopted in July 2010. A number of planning decisions regarding the transition from analogue to digital terrestrial broadcasting were adopted and several international agreements were ratified.

However, implementing rules remain to be adopted to ensure that the switchover process takes place as indicated in the 2009 digital switchover strategy.

As regards audiovisual policy, implementation of the law on public information and its amendments has continued, producing some positive effects such as greater responsibility for distribution companies, founders of media outlets and editors-in-chief as well as increased accountability for breaking the presumption of innocence and violating the rights of minors. However, some provisions of the law include excessive fines for the violation of professional standards and for non-registration of media outlets.

Preparations for a comprehensive media strategy are ongoing. Media legislation remains to be aligned with the Audiovisual Media Services Directive.

Overall, preparations in the area of information society and media have continued. The legislative framework has been strengthened, but implementation remains slow and inadequate market and regulatory developments in the electronic communications sector are of particular concern. Preparations in the field of information society services are moderately advanced. In the audiovisual area, media legislation needs to be aligned with the *acquis*, and a number of provisions of the law on public information continue to raise concerns.

4.2.7. Financial control

Progress has been made in the area of public internal financial control (PIFC). A Central Harmonisation Unit (CHU) was established in the Ministry of Finance in March 2010. Budget inspection was fully separated from the CHU function. A certification scheme for internal auditors has been developed by the CHU, and a committee for the examination and certification of internal auditors in the public sector was established by the Minister of Finance. The Budget System Law was amended to improve alignment with international standards.

However, Serbia needs to continue with the establishment of internal audit units in budget- user organisations and auditors require further training. Managerial

accountability and development of financial management and control are still at early stages. Centralised budget inspection needs to be further developed.

With regard to external audit, in May 2010 the Law on the State Audit Institution (SAI) was amended primarily to allow easier recruitment of audit staff and better salary conditions. The SAI performed a partial audit of the 2008 state accounts and reported to parliament in November 2009. However, the SAI is not yet fully operational and further audit staff needs to be recruited.

Overall, there has been progress in this area, but Serbia is still at an early stage in the implementation of PIFC and external audit.

4.2.8. Statistics

There has been some progress on statistical infrastructure. Cooperation and coordination between the Statistical Office and other producers of official statistics have improved, in particular with the Ministry of Agriculture. A Statistical Council, bringing together representatives from various ministries, has been created. Legislation on statistics, on the agricultural census, the population census and the classification of economic activities, were adopted in December 2009. The Statistical Office was reorganised in April 2010 following a 10% staff cut. However, further budgetary as well as staff resources required for the statistical production remains to be ensured.

Good progress was made on classifications and registers. A substantial effort has been made to develop the statistical business register on which two regulations were adopted in July. There has been some progress towards harmonising the Serbian regional statistical classification with the EU NUTS⁴ Regulation, but a formal agreement still has to be reached with Eurostat.

There has been good progress on sector statistics. Preparations for the census on population and housing are well advanced. Special efforts have been made to involve the Roma population in the census. Preparations are being made for an agricultural census. A pilot agricultural census was conducted in December 2009. National accounts have been further developed. A labour cost survey has been carried out for the first time. Business and Energy statistics have been further developed. However, the budget for the population census is not yet allocated.

Overall, Serbia has made good progress in statistics and is moderately advanced towards meeting the requirements of the European standards. Preparations for the population census are well advanced but its funding remains to be ensured. Further progress is needed in several statistical domains and notably concerning strengthening of the capacity of the Statistical Office.

4.3. Justice, freedom and security

4.3.1. Visa, border management, asylum and migration

Serbia has made progress in the area of visa policy and the wider framework of the visa liberalisation dialogue.

⁴ Nomenclature of Territorial Units for Statistics.

Visa-free travel to the Schengen area entered into force in December 2009 for Serbian citizens holding biometric passports, after Serbia had fulfilled the requirements of the visa liberalisation roadmap. In the first months of the visa-free travel regime with the Schengen countries, increased numbers of asylum seekers from Serbia had been registered in Belgium and Sweden. After the readmission of Serbian citizens, who had filed unfounded asylum applications, and preventive action taken by the Serbian authorities, the numbers have declined. However, a new rise in asylum applications was registered in August and September. The authorities need to continue informing citizens about the rights and obligations stemming from visa-free travel. Allegations of bogus changes of residence of Kosovo residents to Serbia, facilitated by corrupt behaviour of officials, are being investigated by the Serbian authorities.

New visa stickers have been issued since June 2010. The visa-free regime with several former Soviet republics was suspended in July 2010. Serbia maintained a visa-free regime for the citizens of all EU Member States and citizens of Croatia, Bosnia and Herzegovina, the Former Yugoslav Republic of Macedonia and Montenegro.

However, the current list of countries the citizens of which require visas to travel to Serbia is not fully in conformity with the EU *acquis*. Challenges persist for diplomatic missions and consular posts in issuing visas due to limited access to central databases as well as a lack of qualified staff. The validity of old passports has been extended until the end of 2010 due to the limited capacity for issuing new passports.

Overall, Serbia is moderately advanced in aligning its visa policy with European standards there has been some progress in the area of border management. The coordination body for implementing the Integrated Border Management strategy has been established in June 2010. Serbia has continued to improve the infrastructure and equipment at border crossing points and to strengthen security checks on persons, documents and goods. Installation of the TETRA system has progressed, but has not yet been completed. Border police cooperation has continued, with joint patrols with Bosnia and Herzegovina, Hungary and Montenegro. Efforts to further increase the risk analysis capacity of the border police have continued. Serbia has been involved in joint operations and has regular data exchange with Frontex and participates in Western Balkans Risk Analysis Network. The implementation of the working arrangement is satisfactory.

However, border police, customs and phytosanitary services are still lacking operational coordination and cooperation with regional counterparts needs to be improved. Disparities in infrastructure between border crossing points persist, with control of the borders with the Former Yugoslav Republic of Macedonia, Montenegro, Bosnia and Herzegovina and Croatia still showing important weaknesses. Not all border crossings are fully connected to the central database of the Interior Ministry and to the Interpol system (I-24/7). Surveillance and control at the Administrative Boundary Line with Kosovo need to be further strengthened and cooperation and exchange of information with EULEX/Kosovo police improved. Border police is not yet fully staffed and its risk analysis capacity needs to be further strengthened.

Overall, Serbia started to address its priorities regarding border control. Further efforts are needed to eliminate the disparities between individual border crossing points and to improve control at the borders with the former Yugoslav Republic of Macedonia, Montenegro, Bosnia and Herzegovina and Croatia and in particular at the Administrative Boundary Line with Kosovo.

Little progress has been achieved in the area of asylum. In the period from October 2009 to August 2010, 114 asylum claims have been filed. One final decision granting asylum has been taken. The government adopted a list of safe countries for asylum seekers. Subsidiary protection status has been granted in some cases. Reception of asylum seekers, under the competence of the Commissariat for Refugees as a coordination body for integration of asylum seekers, is well organised and functioning.

However, the Asylum Office, the first instance body for asylum claims, has not been established. Claims continue to be processed by the section for asylum in the Border police, which is understaffed. A high percentage of cases are closed before the decision is taken as the applicants leave Serbian territory or disappear. Extension of reception capacities for asylum seekers is currently not planned.

Overall, Serbia's asylum system continues to be moderately advanced.

Serbia has made some progress in migration management. Implementation of the readmission agreement between Serbia and the European Union has continued without significant problems. Implementing protocols with Italy, Hungary, Norway and Switzerland have been ratified; a further two, with Austria and Malta, have been signed.

However, effective implementation of the migration management strategy is lacking due to poor capacity and insufficient coordination of the responsible bodies. An action plan has not yet been adopted. Conditions in reception centres have not improved due to a lack of funding. There are concerns in relation to the standardised entry, exchange and protection of data collected in conformity with the law on foreigners. While a central database on foreigners is still missing, most of the competent authorities are keeping individual registers. Reintegration of returnees needs to be improved.

Irregular migrants (the majority coming from Afghanistan and the Middle East) continue to transit through Serbia, following the main routes from Turkey. They increasingly affect neighbouring EU Member States. From October 2009 to August 2010, charges were filed against some 3400 foreign citizens for illegally entering Serbia. A significant number of persons indicating their intent to file an asylum request at the border never do so, but disappear after entering Serbia in order to stay as irregular migrants or travel further.

Overall, migration management in Serbia continues to be moderately advanced.

4.3.2. Money laundering

Some progress has been made in the area of anti-money laundering. An action plan for the implementation of the strategy has been adopted in October 2009 and a coordination body established. The Administration for Prevention of Money Laundering, which acts as the financial intelligence unit, has held further training events for its staff and carried out awareness-raising activities for reporting entities. Efforts to improve national and international cooperation in the investigation and processing of offences continued. In June 2010, Serbia acquired observer status in the Eurasian group on combating money laundering and financing of terrorism.

However, practical results in the fight against money laundering have remained weak. Cooperation between competent authorities has continued to show shortcomings. The Administration for Prevention of Money Laundering lacks capacity to systematically identify suspicious cases. Guidelines for the identification of

suspicious transactions have not yet been adopted. Reporting remains poor, in particular outside the banking sector, with the real estate sector and currency exchange offices being of most concern. An effective system for monitoring and analysing cash transactions is not in place. The judiciary and law enforcement services lack expertise in handling money laundering cases and financial investigations. Final convictions in money laundering cases remain rare.

Overall, Serbia has started to address its priorities in fighting money laundering, which nevertheless continues to be a cause of concern.

4.3.3. Drugs

Good progress can be reported in the area of fighting drugs. Serbian law enforcement agencies have continued investigations into illegal production, trade and smuggling of drugs and improved international cooperation. The Serbian intelligence agency (BIA) has contributed to the seizure of some 2.7 tonnes of cocaine coming from South America by US and other authorities. Several drug-producing laboratories have been dismantled in Serbia. Between October 2009 and August 2010, Serbian authorities seized some 1,150 kg of drugs, out of which some 930 kg of marihuana and 155 kg of heroin. Operational cooperation between customs services at regional and international level has improved.

The Ministry of Health has continued its awareness-raising activities. Efforts were taken to reduce drug consumption in prisons, including the establishment of five 'drug-free' units, where special measures are taken to prevent drug abuse by inmates.

However, Serbia remains on one of the main Balkan trafficking routes for heroin and synthetic drugs to the EU, and also became more important as a transit country for cannabis. Criminal groups from Serbia are involved in smuggling cocaine from South America to Europe.

A new law on drugs has not yet been adopted. Little progress can be reported in implementing the national strategy and action plan to fight drugs. The National Commission for implementation of the drug strategy has not been established. This adversely affects cooperation and coordination on both the preventive and repressive sides. Serious weaknesses continue to exist in surveillance of the borders with the former Yugoslav Republic of Macedonia, Montenegro, Bosnia and Herzegovina and Croatia as well as the Administrative Boundary Line with Kosovo, which is of particular concern in view of the level of drug trafficking activity in Kosovo. Police and border police are not yet fully connected to the central database on drugs.

A large quantity of seized drugs has still not been destroyed due to alleged environmental concerns. Cooperation with the European Monitoring Centre for Drugs and Drug Addiction needs to be improved.

Overall, preparations in fighting drugs are moderately advanced. Serbia's contributions to the dismantling of international drug trafficking groups and the seizure of important amounts of illegal drugs show clear commitment and operational capacity. However, drug trafficking from and through Serbia remains of concern.

4.3.4. Police

Serbia has made some progress in the area of police reform. Capacity building has continued primarily within specialised services of the criminal police such as the services for combating organised crime, financial investigations and high-tech crime.

Some measures have been taken to improve the methodology and standards of police work, including an information booklet explaining the regulatory framework. Training and education have continued on best practice in police work and on work in communities and with minorities.

Cooperation between various police structures, as well as regional and international cooperation, have improved further, leading to good results in particular in combating drugs trafficking and organised crime. In June 2010, Serbia signed a non-binding roadmap with Europol on the preparations for the conclusion of an operational agreement. Enhanced efforts are necessary to meet the challenges of the roadmap, particularly in areas related to the protection of personal data and classified data.

However, at the level of the Interior Ministry, there is no effective strategic planning and human resource management remains weak. This adversely affects prioritising and budgeting. Intelligence-led policing and the criminal intelligence system need to be improved. The lack of openness and transparency of recruitment procedures and career development within the police remains of concern.

Understaffing and inadequate working conditions for some police services need to be addressed. Further steps have been slow towards developing an efficient internal control system ensuring proactive investigations and monitoring of the legality and conformity with standards of police conduct. Between October 2009 and August 2010, 316 criminal charges were filed against police officers. Security of police officers needs to be improved in the light of the increased number of incidents and attacks on police officers.

The work of the large number of private security agencies remains unregulated, representing a serious security challenge. Illegal firearms and explosives continued to be widespread and subject to trafficking throughout the region.

Overall, the police system remains moderately advanced. The Serbian police have shown investigative capacities, but further sustained efforts are needed.

4.3.5. Fighting organised crime and terrorism

Good progress has been made in fighting organised crime. The action plan to fight organised crime has been adopted in September 2009 and implementation has started. Investigative capacities and the use of special investigative techniques have been further strengthened. Specialised training of the relevant police services has continued. The work of the unit for financial investigations within the organised crime service has continued under the leadership of the Special Organised Crime Prosecutor. Confiscation of assets started in a more systematic way and confiscations were carried out in a number of cases.

Cooperation between relevant agencies has improved within the country, in the region and internationally, leading to good results in a number of high-profile investigations against organised crime groups. In these cases, a number of suspects have been arrested and illegally acquired assets confiscated. In October 2010, an agreement establishing a regional office in Belgrade for improving cooperation in the fight against organised crime was signed with Albania, Bosnia and Herzegovina, Croatia, Montenegro and the Former Yugoslav Republic of Macedonia.

Cooperation with Eurojust improved and Serbia established additional contact points. A meeting with Eurojust representatives took place in May 2010 in order to

prepare negotiations for a cooperation agreement. Protection of personal data and of classified data is key for successful conclusion of such an agreement.

However, a new and substantially revised Criminal Procedure Code has still not been adopted. The Commission for Inter-ministerial Coordination in the field of Justice and Home Affairs has shown little activity. The capacity of the specialised police services to conduct proactive investigations and engage in intelligence-led policing remains limited due to understaffing and lack of analytical expertise. The number of final convictions remains low.

The lack of adequate control and surveillance of the administrative boundary line with Kosovo continues to be problematic in an area which is vulnerable to organised crime activities. Cooperation, implementation of the police protocol and exchange of relevant information with EULEX need to be further improved. A uniform database on organised crime cases is still missing. Inter-service cooperation, including between the tax administration, customs and the Administration for the Prevention of Money Laundering, needs further improvement. Witness protection needs to be improved. The limited capacities of the agency for the management of seized assets and the fast auctioning of seized assets in the absence of a conviction or any risk of immediate deterioration raise some concerns.

Overall, Serbia has started to address its priorities in fighting organised crime. Recent results in investigating organised crime activities at national and international level and in the confiscation of illegally acquired assets are encouraging, but need to be followed up by transparent, impartial and effective proceedings in the judiciary. The capacities of the law enforcement agencies to use modern investigative techniques, in particular in the area of financial investigations, need to be further strengthened.

Serbia has made some progress in fighting trafficking of human beings. Procedures to identify victims have been adopted and the number of identified victims has continued to increase, while the regional trend points towards a decrease in trafficking of human beings. Law enforcement authorities remained active and regional and international cooperation improved further. From October 2009 to August 2010, 94 victims of human trafficking have been identified, with women representing the majority. These victims, mostly of Serbian origin, had been trafficked for sexual abuse, begging, forced marriages, and labour exploitation. Awareness-raising activities have continued.

However, ratification of the European Convention on Action against Trafficking in Human Beings has not been followed by further measures to guarantee its effective implementation. The strategic framework, which includes the strategy and action plan for fighting trafficking in human beings, but also the migration management, the irregular migration and the organised crime strategies, needs to be amended to allow a better policy response to emerging trends and improved cooperation between the police, prosecution and courts. As far as the protection of victims is concerned, more needs to be done to provide them with comprehensive assistance and reintegration. Although some emergency funds have been secured for two shelters run by NGOs, overall funding for NGOs active in the field of prevention and support to victims and for the government's protection agency remains unsatisfactory. NGOs continue to rely heavily on international donor funds.

Overall, Serbia is moderately advanced in fighting trafficking in human beings.

Serbia has made some progress in the fight against terrorism. The law regulating the military intelligence and military security agencies was adopted in October 2009, providing for better cooperation between agencies in the fight against terrorism. Implementation of the amended law on the prevention of money laundering and the financing of terrorism has started. Capacities of the law enforcement authorities in this area are generally good.

However, following the ratification of the relevant Council of Europe Conventions, no prevention policies or legislative and institutional changes were adopted for further alignment with these provisions. A specific list of terrorist suspects has not yet been established.

Overall, Serbia is moderately advanced in fighting terrorism.

4.3.6. Protection of personal data

There has been little progress on protection of personal data. The Strategy for the Protection of Personal Data has been adopted in August 2010. The office of the Commissioner for Free Access to Information of Public Importance and Personal Data Protection, which acts *inter alia* as supervisory authority for the protection of personal data, was allocated additional staff.

However, the Law on the Protection of Personal Data is not fully in line with EU standards and not all necessary implementing legislation has yet been adopted. The office of the Commissioner for Information of Public Importance and Personal Data Protection continues to lack financial and human resources. This raises concerns over its capacity to adequately carry out its supervisory tasks.

Overall, the protection of personal data in Serbia remains moderately advanced. Personal data protection is a key precondition for Serbia to conclude an agreement with Eurojust and an operational agreement with Europol.