

Annex

Annual Action Programme for 2005 for Community
Assistance to the former Yugoslav Republic of Macedonia

1. Identification

Budget heading:	19 07 01 Assistance for the Countries of the Western Balkans
Total cost:	EC contribution: €34.5 million
Legal basis:	Council Regulation 2666/2000 as amended by Council Regulation (EC) 2415/2001 (CARDS)
Annual programming/ implementation:	European Agency for Reconstruction €25.2million; Commission headquarters (Tempus, Customs and Decentralisation of management of assistance projects and Community programmes) €9.3 million

2. Country update

The period of 2004 was marked by a general **political stability** in the former Yugoslav Republic of Macedonia, although there was a stir of events in the summer and early autumn caused by reaction in some quarters to the new Law on Territorial Division, an integral part of the decentralisation process that underpins the Ohrid Framework Agreement (see below).

The accidental death of President Trajkovski in February was handled calmly, and the subsequent presidential election was conducted without major incident. The election resulted in a consolidation of the ruling coalition's power: the Prime Minister, Branko Crvenkovski, won the presidency and a new government was formed by the Minister of the Interior, Hari Kostov. Most ministers from the previous government kept their portfolios and the coalition with the ethnic Albanian party DUI remained intact. However, problems appeared later in the year when the Prime Minister Hari Kostov resigned due to "disagreements within government". The ruling SDSM party has chosen a new party leader, the former Minister of Defence Vlado Buckovski, who has been given the mandate to form a new coalition government. The new government, with Buckovski as a Prime Minister, was officially elected by the Parliament in mid-December 2004.

One of the main events in 2004 was the referendum on the issue of the new Law on Territorial Division, that led to protests by the ethnic Macedonian population in certain mixed ethnic municipalities. However, despite some evidence of a growing opposition to the new Law and to the redrawing of municipal boundaries, the referendum held on 7 November resulted in a low voter turnout - way below the 50% needed - and as such the Law on Territorial Division remained in place. The critical challenge now for the Government is to ensure that decentralisation – and the raft of complex legislation that has been adopted in this area – is actually implemented on the ground in 2005. In many cases, municipalities are far from ready to take on their newly devolved responsibilities and central ministries remain unsure of their role in the process.

In terms of public mood, some analysis of the November referendum showed that the dissatisfaction manifested over the issue of new municipal boundaries was, to a large extent, derived from the poor socio-economic situation in the country and the general dissatisfaction of the public regarding their living

standards and future prospects⁽¹⁾. Opinion polls continue to show that unemployment and poverty are the most pressing problems for the population and both could, in the long run, have a negative effect on stability in the country. The realistic unemployment is difficult to assess due to the extensive grey economy and rules for accessing health benefits, but current official figures put the level of unemployment at 36.7%⁽²⁾.

The trends which have characterised the former Yugoslav Republic of Macedonia's **economic performance** since independence have continued over the recent period. A mixed picture emerges: notable achievements in macroeconomic management counterbalanced by slow progress in the area of key structural reforms. On the macro-economic side, inflation has been brought down to single figures in recent years and by the end of 2004 there was a deflationary rate of -0.4%. Complementing this trend, sound fiscal policy has helped gradually lower the level of government debt to under 40% of GDP.

However, the government's positive fiscal management is not reflected in the structure and performance of the economy. Negative economic indicators persist, the most important of which is the weak and uncompetitive corporate sector. In the first half of 2004, the IMF reported a 3.6% decline in the level of GDP. There is a lack of corporate development, poor liquidity in the business sector, and an absence of foreign and domestic investments.

The trade deficit, which compared to 2002 and 2003, when it stood at about US\$ 800 million, is estimated to reach US\$ 1.2 billion by the end of 2004, which is a 50 percent year on year increase. This year's trade deficit will be the highest ever since the country gained independence. The industry of the former Yugoslav Republic of Macedonia has not been restructured in a manner that would allow for its revitalisation and there is no increase in the level of exports. The export base of the former Yugoslav Republic of Macedonia has not expanded since independence in 1991. The economy failed to catch up with the other countries in transition in terms of creating new export-oriented companies.

One serious impediment to investment, domestic and foreign, is the tardiness of the court and other administrative procedures required for registering new economic entities. The bankruptcy and liquidation procedures are amongst the most complicated and lengthy in Europe. A challenge for the Government in the years ahead will be to deliver on difficult structural reforms in the public administration, labour market, and judiciary. These will be critical for the creation of a more favourable business climate and to enhance foreign direct investments; at present the former Yugoslav Republic of Macedonia is assessed as having the second lowest level of foreign direct investment in Europe⁽³⁾.

The issue of **inter-ethnic relations** has been addressed by the Government since the end of the crisis in 2001 with full implementation of the Ohrid Framework Agreement being a stated priority. Some 24 new laws have been

¹ Early Warning Report, UNDP, November 2004

² Source: State Statistical Office

³ Source: UNCTAD

adopted which directly address issues relating to equitable representation and use of languages. Implementation will be the key challenge but in terms of moving towards more equitable representation in the public service, the Government has already set a first target of reaching a non-majority community representation of 14% in the public administration. Unlike the opposition to new territorial division, there has been little public reaction to new legislation addressing the use of languages and equitable representation, which is a reassuring trend. That said, one of the biggest challenges remains for the Government to ensure all groups in society have an equal stake in the economic development of the country, as much as possible mitigating the social tensions that can easily arise from high unemployment and low economic livelihood.

3. Summary of the action programme

The proposed 2005 Annual Programme for the former Yugoslav Republic of Macedonia focuses on three key areas of support: democratic stabilisation, good governance and institution building and economic and social development. The programme has been developed in the strategic framework set out in the Country Strategy Paper (CSP) 2002-2006 and the draft Multi-annual Indicative Programme (MIP) 2005-2006. The programme also seeks to reinforce the priorities of the Stabilisation and Association Agreement and the European Partnership – the key strategic documents on the former Yugoslav Republic of Macedonia's path to EU accession, and support the implementation of the Ohrid Framework Agreement.

The programme has been developed and will be implemented in close co-operation with the Government of the former Yugoslav Republic of Macedonia, key donors, and International Financing Institutions (IFIs). In the development of the programme, due attention has been paid to ensure complementarity and synergies with other assistance programmes, in particular those of EU Member States and CARDS regional initiatives, and with IFI lending programmes.

The programme is summarised in the sections that follow, according to the headings outlined in the MIP. Further details are available in a separate set of project fiches.

3.1 Democratic stabilisation (approx €2 million)

The programme in the area of Democratic stabilisation focuses on assistance to the Government with the further implementation of the Framework Agreement.

3.1.1 Minority rights (approx €2 million)

Background and cooperation related policy of Beneficiary country

The implementation of the Ohrid Framework Agreement remains one of the key priorities of the Government of the former Yugoslav Republic of Macedonia in 2005. The signing of the peace deal in August 2001 set in train a series of Constitutional amendments and new laws to reflect the principles and

requirements of the Framework Agreement. The primary focus of the Framework Agreement is on decentralisation, non-discrimination and equitable representation, special parliamentary procedures, education and use of languages, and expression of identity.

Whilst the process of implementation of the Agreement is somewhat delayed compared to the original timetable, major progress has been made over the past two years. The Constitution has been changed, around 24 laws have been adopted, and a long series of practical reforms have been enacted. After the adoption of the constitutional amendments and most of the key laws required by the Framework Agreement, the Government's focus has increasingly turned to two of the most far reaching provisions of the Agreement, namely, decentralisation and equitable representation. In addition, the Government needs to ensure that there is now real implementation of new or amended legislation that has been adopted in the last two years.

With a view to achieving a more comprehensive approach to implementation of the Framework Agreement, the Government adopted an Action Plan in April 2003. Accordingly, one of the Deputy Prime Ministers was charged with overseeing co-ordination of implementation of the Framework Agreement, with a new Sector for Implementation of the Framework Agreement being established in the Deputy Prime Minister's office in April 2004. One of the new Sector's tasks is to ensure that adequate finances and human resources are devoted to implementing the Framework Agreement. But the Sector is still in its infancy and technical assistance and training is needed to ensure that it can fully take on its new role, especially in ensuring adequate resource allocation in line with agreed priorities.

Integral to the work of the new Sector, there is a continued need for the Government to address one of the more complex and politically sensitive elements of the Ohrid Framework Agreement: equitable representation. The principle of equitable representation of all communities in the public service is a crucial step in enabling the state to serve all groups in the country and thereby improving citizens' identification with the state. There has been some progress and the Government has made provisions in the public sector budget for posts for non-majority civil servants. However, there is still a long way to go in terms of securing full equitable representation and further work is needed particularly in attracting more high-potential civil service trainees from ethnic Albanian as well as other non-majority groups.

Coherence with EC cooperation policy and the MIP

The programme will assist the former Yugoslav Republic of Macedonia to implement the European Partnership priority of ensuring there is in place a viable plan for equitable representation in the public sector and, more widely, the means for the Government to fully implement the Ohrid Framework Agreement. This has been repeatedly emphasised by the Commission in its dialogue with the Government on progress in the Stabilisation and Association process.

Identified projects

3.1.1.1 Implementation of the Framework Agreement (approx €2 million)

The project will aim to strengthen the capacity of the Government to take forward full implementation of the Ohrid Framework Agreement. In this respect, the project will work in two areas: development of the capacity of the Government's new Sector for the Implementation of the Framework Agreement, and increase of the representation of non-majority ethnic groups in the public administration. The first project component will entail technical assistance and training for the Sector for Implementation of the Framework Agreement. The second project component will provide training for high-level (category I) civil servants from minority communities. It will follow the on-going CARDS projects that are providing training for category III and II civil servants from minority groups in the country.

3.2 Good governance and institution building (approx €18.5 million)

The proposed Good governance and institution building programme targets two broad areas: Justice and Home Affairs (JHA) and public administration reform. The JHA interventions focus on further support of the judicial and police reforms and in combating organised crime. The projects proposed in the domain of public administration reform include: administrative capacity building in the areas of statistics and telecommunication, as well as capacity building of country's authorities with a view of the eventual transfer of the management of Commission's programmes post-2006, further support to the decentralisation process and assistance in the area of customs and taxation.

3.2.1 Justice and home affairs (approx €3.5 million)

Background and cooperation related policy of Beneficiary country

Due to its geographical location, the former Yugoslav Republic of Macedonia has always been a transit route for the movement of goods and people, legal and illegal. Criminal activities, including trafficking in persons, drugs, munitions and contraband materials are widespread. Within the country, politically motivated criminal activity is also encountered along with corruption in the private and public sectors. Moreover, from a security aspect, parts of the country continue to be only tenuously policed, in part a consequence of unresolved tensions from the crisis of 2001. Kidnappings, hostage situations and armed resistance to arrest are encountered periodically and the law enforcement agencies are both inexperienced and poorly trained to respond in an efficient and effective manner.

Within this context, it is a matter of concern that the Rule of Law and the ability of the law enforcement agencies to properly exercise and execute it continue to be weak in the former Yugoslav Republic of Macedonia. The Government's own draft Judicial Reform Strategy (September 2004), states that the country has, since independence in 1991, experienced a "series of weaknesses and

inconsistencies in the transition to a modern democratic and legal state, hence the need to intensify the reforms in all segments....” Integral to this process is the need to take forward reform strategies in the judiciary and police.

Despite these weaknesses, the Government has made progress. A Police Reform Strategy was finally adopted in February 2004 and is now in the early stages of implementation with EC CARDS assistance. A new Judicial Reform Strategy was drafted and adopted by Government, but detailed action plan is yet to be developed. In short, there appears a willingness on the part of Government to take forward both reform strategies, although a number of concrete steps are needed to ensure implementation.

In the case of the police, the Reform Strategy addresses the key issues within the police service related to organisational and management structure. The aim is to achieve a more flexible and modernised police service, better adapted to serving the community and dealing with the challenges posed as well as organised and other serious crime. In this vein, the national authorities are seeking assistance in enhancing the police operational effectiveness in key areas, including response to violent crime and other emergency situations. At present, the police is poorly equipped to respond effectively in such extreme circumstances. The reforms currently being undertaken at a policy level in the police therefore need to be accompanied by improvements in operational capacity, particularly in dealing with organised crime and emergency situations.

In the judiciary, the reform process is still more in its infancy. A number of themes of the draft Judicial Reform Strategy echo those of the Police Reform Strategy, including the need for greater transparency and merit-based recruitment, selection and promotion, disentangling this from the political process. But the Strategy also highlights areas where the effectiveness of the judicial process needs to be enhanced in detecting and prosecuting organised crime. In this vein, two new laws have been passed in 2004 which greatly strengthen the position of the Public Prosecutor’s Office (PPO) in dealing with organised crime and corruption. The new Law on Public Prosecution and Law on Criminal Procedures provide for the establishment of a new Department for Prosecution of Organised Crime and Corruption within the PPO. Moreover, a much greater role is envisaged for the public prosecutors in pre-trial investigation. The legal framework is in place but assistance is needed in helping the Public Prosecutor take on the new responsibilities in investigating and prosecuting serious crime and corruption.

A similar pattern emerges in consideration of the provisions and mechanisms in place for dealing with money laundering. A new Law on Money Laundering Prevention was passed in July 2004, which set up a new Directorate for Money-Laundering Prevention (DMLP) within the Ministry of Finance. The Directorate is in the lead for investigating and reporting on financial crime and has the power to demand information from all financial sectors – banks, stock exchange, trade and venture capital companies – as and when it sees appropriate. New supervisory mechanisms are set up in all financial sectors. However, as with the new Department for Prosecuting Organised Crime and Corruption in the Public

Prosecutors Office, assistance is needed to properly establish and develop the DMLP and enable it to exercise its functions in accordance with the new Law.

Coherence with EC cooperation policy and the MIP

The JHA programme proposes a series of projects that directly address issues in the fight against organised crime, corruption and money laundering set out in the MIP 2005-2006. The programme reinforces key articles of the Stabilisation and Association Agreement (SAA) as well as the new European Partnership. The work with the Public Prosecutor's Office will directly support Article 74 of the SAA, focusing on overall reform of the judicial system, as well as reinforce those priority areas of the European Partnership calling for a strengthening of the institutional capacity of the prosecutor's office. In a similar manner, strengthening the operational capacity of the police is a key element of the Government's own Police Reform Strategy which directly addresses Articles 74 and 78 of the SAA. Finally, the assistance to the DMLP will reinforce implementation of Article 77 of the SAA which refers to co-operation both within state and across borders in combating financial crimes. The project will also address those medium-term priorities in the European Partnership which call for increased legal and administrative provisions in the fight against economic and financial crime and fraud.

Identified projects

3.2.1.1 Support to Public Prosecutor's Office (approx €1.5 million)

The overall objective of the project is to develop a fully independent Public Prosecution service in the former Yugoslav Republic of Macedonia which is well placed to efficiently and effectively exercise the rule of law in cases of organised crime. The project will aim to assist the Public Prosecutor's office in taking forward its new responsibilities related to investigation and prosecution of organised crime and corruption. Technical assistance will be provided to the Public Prosecutor's Office to help in the establishment of the new Department for Prosecuting Organised Crime and Corruption, as set out in the Government's Action Plan for the Public Prosecutor's Office. The project will also provide training for public prosecutors, their deputies and administrative staff in fulfilment of their new roles and responsibilities assigned with the new Laws.

3.2.1.2 Combating money laundering (phase II) (approx €1.5 million)

The project will continue the advisory support to the Directorate for Money Laundering Prevention (DMLP) and reporting institutions that is currently being provided under CARDS 2002. The overall intervention will aim to contribute to the establishment of a fully functioning system that would prevent money laundering and terrorism financing. In this respect, the project will provide assistance and capacity building for the DMLP. Another key component of the project will be the establishment of effective co-operation mechanisms between DMLP, reporting institutions, law enforcement, criminal justice and regulatory authorities. Project activities will include:

- Assistance in drafting and passing legislation and regulations compatible and in line with norms and standards prevalent in EU Member States.
- Assistance in the definition of training requirements, delivery of training and/or supervision of the delivery of training for the DMLP and reporting institutions.
- Assistance in the specification of procedural and technical solutions to operational requirements.

3.2.1.3 Strengthening capacity to combat organised crime and terrorism (approx €0.5 million)

The project will aim to contribute to the establishment of a fully functioning police service which is able to effectively and efficiently respond to serious crime and emergency situations. It will work to develop the capacity of the police to better execute arrests and to better respond to emergency situations, such as kidnapping, hostage and terrorist incidents. This intervention will complement the restructuring and training support for the Police Special Tasks Unit initiated under French bilateral assistance. More specifically, the project will address the equipment needs of the new Special Tasks Unit, in order to enable this unit to function in line with the new structures and EU standards.

3.2.2 Public administration reform (approx €15 million)

Background and cooperation related policy of Beneficiary country

Two of the biggest challenges facing the Government in the area of public administration relate to further alignment of the legislation and structures with the EU requirements and realisation of the decentralisation process. Both processes are fundamental to the country's progress on the path to Stabilisation and Association and fulfilment of the Ohrid Framework Agreement. Yet there continues to be a lack of institutional capacity in key areas of Government to effectively take forward the necessary reforms.

Administrative Capacity Building

Statistics

The State Statistical Office (SSO) is the main provider of non-financial statistics in the country. It has an independent status within the Government, which is defined by the Law on State Statistics from 1997. It is responsible for the drafting of overall statistical programs, which are compiled for five-year periods. The current programme covers the period 2003-2007 and addresses the whole National Statistical System, including eight different data providers. The internal organisation of the SSO was reformed in 2004 and includes nine sectors at a central level and well-developed network of regional offices.

In 2004 EUROSTAT and UN-ECE⁴ carried out the second joint "Global Assessment of the Statistical System of the former Yugoslav Republic of

⁴ UN-ECE – United Nations - Economic Commission for Europe

Macedonia". The report highlighted the progress in the areas of provision of programming, planning and priority setting frameworks, dissemination policy and IT environment. However, it also stressed the need for the SSO to strengthen its institutional capacity within the government, the inter-ministerial consultation and consultation with users, as well as its cooperation with the local government. Furthermore, this report identified a number of short- and long-term priorities for country's statistical system, which the SSO is now aiming to implement.

Telecommunications

The telecommunications sector is currently regulated by the Act on Telecommunications adopted in 1996 and modified in 1998, as well as by other acts and regulations that define more precisely this field. Although the Government has included the area of electronic communications in the national priorities since 2002, the progress has been rather slow until recently. In late 2004 a new Law on Electronic Communications has been prepared to comply with EU legislation and provide adequate options for liberalisation of the telecommunications market. It was reviewed by EU expertise and is to be adopted by the Parliament by mid February 2005. The Law foresees the establishment of an Independent Regulatory Body for Electronic Communications to oversee sector development. This body will take on the regulatory functions, which are now under responsibility of the Ministry of Transport and Communications (MTC) – the institution currently governing the issues in the area of telecommunications. After the establishment of the Regulator, technical assistance will be necessary in order to provide legal and institutional EC expertise related to enforcement of the legislation, which is critical to develop institutional capacity to implement the new legal provisions and stimulate sector growth fostering attraction of investment and improvement of the technological infrastructure.

Decentralisation of the management of assistance

Since 2002, the EC assistance programmes to the former Yugoslav Republic of Macedonia have been managed by the European Agency for Reconstruction. However, the Government strongly feels that the management of the assistance should be transferred to the national authorities and has therefore been consistently approaching the EC with requests for decentralisation of CARDS management. Prior to taking the final decision on the introduction of a decentralised system, a number of steps need to be undertaken, including thorough assessment of the current capacity of relevant institutions, addressing the identified gaps, and capacity re-assessment in order to ensure that all necessary requirements for introduction of a decentralised system of management of the assistance are met.

Decentralisation

Alongside the Stabilisation and Association process, the Ohrid Framework Agreement continues to be the guiding framework for the Government, defining its strategic priorities in the years ahead. In this context, devolution of powers from central to local government is one of the main priorities determining Government policy across a range of sectors.

The new Law on Local Self-Government, adopted in January 2002, set out those competencies to be devolved to local government level. Following this Law, a package of other decentralisation laws was adopted by the Government in August-September 2004. These included the Law on Local Government Finance; the Law on Territorial Organisation of Local Self-Government; and the Law on City of Skopje. The new Law on Territorial Organisation of Local Self-Government foresees a considerable reduction in the number of municipalities, from 124 to 84, and enhancement of their authorities. The new municipalities will have the power to take decisions in areas such as education, health, culture, urban planning and local policing. In parallel, the central government will have to develop supervision and co-ordination mechanisms aimed at making policy adjustments and further decentralisation of functions to the municipalities.

As it did for managing the European integration process (above), the Government adopted an operational plan for decentralisation. The Operational Programme for Decentralisation of Power sets out the major areas of legislation, primary and secondary, required to underpin decentralisation and details the steps in the transfer of powers from central to local government. Similar to the European Integration strategy, there is a need to assist the relevant ministries to take forward the Decentralisation Operational Plan, in particular the Ministry of Local Self Government. The capacity of central ministries to implement and supervise the transfer of competencies to municipalities is currently lacking, as is the ability of the municipalities to effectively take on the devolved functions. Assistance is needed for both tiers of government to facilitate the decentralisation process.

Finally, in parallel with strengthening the capacity of the municipalities, there is also a continued need to enhance the standard of services and amenities in municipalities through investment in local infrastructure. The small-scale infrastructure needs in the country are estimated to be around €600 million. Helping local municipalities address this need is a crucial element in bringing decentralisation closer to the citizens, enabling municipalities to take decisions on public investment and to improve local amenities.

Customs

An area of the public administration that has undergone significant changes in the last year or so has been the Customs Authority of the former Yugoslav Republic of Macedonia (MCA). These changes have been part of an EC funded programme (CAFAO), which has been helping take forward the process of modernisation of the MCA since 2003.

Customs remains important as a source of revenue (including VAT on importation) but also for public safety (eg. smuggling of illicit drugs etc). In the past, the MCA was characterised by endemic corruption and, as such, any donor funded reform programme became largely redundant. With a new administration in place in 2003, a new reform programme within the MCA became possible. New management techniques have been introduced and EU

Customs and Taxation Blueprints, originally developed for use by the Enlargement States, are to be applied to the context of the the former Yugoslav Republic of Macedonia. The impetus for reform that started in 2003 now needs to be maintained if the progress already made is not to be lost. Improvements in operational effectiveness – for which there has been some notable successes during the last year – needs to be accompanied by sustainable methods for tackling corruption in the customs service.

Coherence with EC cooperation policy and the MIP

The programme will address key MIP 2005-2006 priorities outlined in the sections on administrative capacity building and decentralisation. Moreover, the programme on administrative capacity will contribute to implementation of SAA Article 82 on cooperation in the area of statistics and Article 95 on electronic communications infrastructure and associated services. For the decentralisation programme, several priorities of the European Partnership are addressed which are cited in the Chapter on Implementation of the Framework Agreement. The European Partnership priorities included under the chapter for sector policies – telecommunications are also addressed. The programme on reform of the MCA will directly address the MIP objectives in the area of customs and taxation reform. In addition, Articles 88 and 89 of the SAA are supported by the project.

Identified projects

3.2.2.1 Support to the State Statistical Office (approx €1 million)

This project will aim to enhance the reform of the statistics system in the country and to strengthen the institutional capacity of the SSO at central and local level, through provision of technical assistance and training. The activities will focus on: (i) capacity building of the State Statistical Office; (ii) harmonization of national accounts to EU standards; (iii) improvement of the statistical programme, with a particular focus on business and social statistics; (iv) strengthening of the Information and Communication Technology (ICT) capacity of the SSO; (v) strengthening of the performance and quality monitoring practices in the SSO; (vi) enhancing the overall consultation, cooperation and communication strategy of the SSO vis-à-vis the other public stakeholders, the end-users and the media.

3.2.2.2 Technical assistance to the telecommunications sector (approx €1 million)

The overall objective of the project is to assist in the establishment of a market-based legal framework and regulatory infrastructure for the promotion of an efficient electronic communications sector in the former Yugoslav Republic of Macedonia and to assist the government in creating a competition-based domestic electronic communications market in compliance with EC Acquis and EU best practice and regulations. The main project activities will include: (i) assistance with the drafting of secondary legislation, institution building and training; (ii) capacity building for the MTC; (iii) strengthening of the capacity of

the new Independent Regulatory Body for Electronic Communications; and (iv) awareness raising on the electronic communications sector developments.

**3.2.2.3 Capacity building in support to the decentralisation of management of assistance (approx €1.3 million)
(COMMISSION MANAGED)**

The project will aim to develop the capacity of the national authorities of the former Yugoslav Republic of Macedonia with a view to the future decentralisation of the management of the EC assistance programmes. It will entail two phases. The first phase the project will provide an in depth assessment of the current administrative structures and their readiness to assume the responsibility for the decentralised management of assistance. The subsequent second phase will assist the authorities of the former Yugoslav Republic of Macedonia to establish or upgrade the structures necessary to implement EC assistance under the decentralised implementation system.

3.2.2.4 Support to the decentralisation process (approx €2 million)

The project will aim to support the Government in the process of implementation of requirements of the Ohrid Framework Agreement related to decentralisation. Assistance will be provided at a central Government level with the transfer of competencies to the municipalities. The project will also work with relevant line ministries, in particular with the Ministry of Local self-Government, in order to help them in the process of devolution of specific responsibilities to municipalities, as well as with the subsequent supervision of the newly devolved competencies. Finally, the project will work with the municipalities to enhance their capacity to absorb the transferred competencies.

**3.2.2.5 Development of local infrastructure (phase II)
(approx €6.7 million)**

This project will provide further support to the decentralisation process. It will work at a municipal level and will aim to strengthen municipalities provision of services and amenities through improvement of their infrastructure. This intervention will follow the extensive support that EC has already provided to local infrastructure development – a programme that has been particularly well received by the local authorities. A number of small-scale infrastructure projects submitted by different municipalities will be selected and implemented. To complement these efforts, the project will also provide on-the-job training for municipalities and the Ministry for Local Self-Government on management of infrastructure projects. Furthermore, the project will assist with the development of a plan for improving the production of reliable statistic data on existing needs of the municipalities and other relevant issues.

3.2.2.6 Customs and taxation (approx €3 million) (COMMISSION MANAGED)

The project will provide further assistance to the Macedonian Customs Authority in modernising and developing the service in line with EU Customs and Taxation Blueprints. A number of management areas will be targeted in the customs service including human resources development, development of strategic business plans, and strengthening of enforcement capacity. On the taxation side, the project will carry out a gap-analysis based on EU Taxation Blueprints in order to identify future areas for assistance. Significant in this respect will be compliance control and enforcement with a view to improving revenue yields.

3.3 Economic and social development (approx €10.6 million)

The proposed programme in the area of economic and social development will include: projects targeted at the improvement of the investment climate in the country; joint projects with EBRD and EIB in the areas of transport and environment; further support to the strengthening of the environmental management; continuation of the support to the higher education through the TEMPUS programme; and further assistance with the reform of the employment policies in the country.

3.3.1 Investment climate (approx €3.6 million)

Background and cooperation related policy of Beneficiary country

In the transitional period, the performance in the economy of the former Yugoslav Republic of Macedonia has varied, suffering serious setbacks due to the instability in the region and in the country, as well as due to the slow reform pace. The economy was particularly affected by 2001 security crisis, when the output contracted by 4.5% and the investment activities significantly dropped. The recovery from this situation has been rather slow and four years later the economy of the country is still under-performing and the unemployment level remains high. Moreover, domestic and particularly foreign investments in the country have been declining. This low level of inward investment is the biggest point of concern for the former Yugoslav Republic of Macedonia's economy.

In 2002, gross investments in the country reached 16% of GDP, while the experience of other transitional economies has shown that ambitious economic development is marked with a level of investments at some 25% of GDP. In the absence of sufficient domestic initiative and financial resources, the attraction of foreign direct investments (FDI) is crucial for the accelerated growth of country's economy.

According to the Statistical Bureau and the National Bank, the cumulative value of FDI in the country at the end of 2002 was equivalent to approximately US\$ 912 million, the majority being accounted for by privatisation deals. The most significant investors to date have been Greece, followed by Switzerland, Germany, Hungary, Austria and Slovenia. The majority of foreign investments

were in the manufacturing and construction sectors, but more recent in-flows have focused on the service sector, including banking, insurance and telecommunications.

A recent FIAS report⁽⁵⁾ has shown that the former Yugoslav Republic of Macedonia “had been a relatively poor performer in terms of FDIs, with net FDI inflows under 1% of GDP throughout most of the 1990s”. Some positive developments were encountered in 2000 when FDIs reached 5%⁽⁶⁾ of GDP, and in particular in 2001 with FDIs amounting to 13% of GDP. However, this trend was associated with large privatisation deals. Upon the completion of the privatisation process, the FDI level in 2002 significantly dropped at some 2% of GDP. In 2003, the former Yugoslav Republic of Macedonia was classified by UNCTAD as the country with second lowest FDI level in Central and Eastern Europe⁽⁷⁾.

A number of factors have contributed to the generation of this unfavourable investment outlook. The regional instability has certainly been a very important aspect that negatively influenced the investments; however, there have been many internal factors that further hampered the investment climate in the country. One of the key obstacles to attracting investments have been the administrative procedures and practices, set out in a manner that allows for corruption, favouritism and anti-competitiveness. In general, the business community has a low level of trust in the ability of the Government to articulate and maintain a business-oriented approach that is free of political influences.

Such unfavourable environment for business operations has also negatively influenced domestic investments. Most of the enterprises in the former Yugoslav Republic of Macedonia are of small and medium size (out of some 40,000 registered companies in the country over 95% are SMEs), which experience additional constraints in their work, such as access to finance, high level of taxation, bureaucracy, and insufficient support structures or measures.

Although a number of credit lines for SMEs have been made available by different donors, including the EC, the actual access to financial facilities remains weak and further improvement to the institutional, legal and fiscal environment is needed. Another constraint to SME development that would lead to more domestic investment is the procedure of company registration, which remains the most noteworthy bureaucratic impediment. Business registration and licensing regimes are characterised by a disorganised and decentralised system involving a variety of government institutions and agencies and applying complicated regulations. Businesses are currently required to visit a number of institutions during the registration process, and receive different numbers for court, statistical, and tax registration. The court procedures are extremely slow and complex. Moreover, ownership rights are not well regulated. Unclear property rights constrain collateral and mortgage financing and act as an

⁵ “Administrative procedures for doing business in Macedonia” – FIAS, June 2003

⁶ Source: National Bank of the former Yugoslav Republic of Macedonia

⁷ Out of 19 countries in Central and Eastern Europe, the former Yugoslav Republic of Macedonia ranks 18 in terms of amount of FDI, just before Moldova, ranking last - UNCTAD World Investment Report 2004, September 2004

impediment to the private sector activities. Inexistence of modern real estate cadastre and modern and transparent processes for title transfer and permits also stand among the principal sectoral constraints.

The Government of the former Yugoslav Republic of Macedonia recognises the importance of investments in stimulation of economic growth, as well as the existence of a number of barriers that hamper the attraction of investments in the country. Some steps in addressing this issue have already been taken. In 2003 the Government adopted a "Programme for stimulating investment in the Republic of Macedonia with special emphasis on foreign direct investments in the country." In line with this programme, a Law on Agency for Foreign Investments in the former Yugoslav Republic of Macedonia has been adopted in July 2004, which makes provisions for the establishment of an institution that would work on promotion, stimulation and improvement of investments in the country. Until this institution is officially established, these responsibilities are covered by the Sector for Foreign Investments within the Ministry of Economy. Moreover, to stimulate the SME sector, in April 2003 the Government adopted a "Programme of measures and activities to promote entrepreneurship and competitiveness of SMEs". The SME Department within the Ministry of Economy is charged with the implementation of this Strategy. To support the part of the Strategy related to entrepreneurship promotion, an Agency for Entrepreneurship Promotion was established in May 2004.

These developments have been a positive indicator for the future improvement of the investment climate in the country. However, the challenge is now to ensure sound implementation of the new programmes and laws aiming to stimulate the investments. The improvement of consistency, transparency and accountability across all agencies that interact with businesses will be instrumental to creating a more favourable investment climate in the country.

Coherence with EC cooperation policy and the MIP

Improvement of a framework for investment promotion and protection in the former Yugoslav Republic of Macedonia is an integral part of the Stabilisation and Association Agreement. Article 84 of the SAA in particular addresses this requirement. In addition, Article 86 outlines the need for development and strengthening of the private sector and SMEs.

The implementation of the measures for reduction of barriers to investments outlined in the abovementioned FIAS report has been identified as a medium-term priority of the European Partnership. Development of non-financial SME support mechanisms is also a priority of the Partnership. Moreover, enhancement of the investment climate, including improvement of the business regulatory environment and SME development, are an integral part of the both national and regional MIPs 2005-2006. The programme will also support the completion of the implementation of the European Charter for Small Enterprises.

Identified projects

3.3.1.1 Improvement of the investment environment in the former Yugoslav Republic of Macedonia (approx €1.2 million)

The project will aim to improve the investment climate in the country through assisting the Government with the reduction of barriers to investments and the establishment of effective and efficient institutions for promotion of foreign investments. In this respect, the project will focus on: (i) capacity building for the Foreign Investment Agency of the former Yugoslav Republic of Macedonia (FIARM), and (ii) provision of technical assistance to the Sector for Foreign Investments (SFI) within the Ministry of Economy. The first component of the project will assist with the development of the organisation structure and strategic plan for FIARM. It will also help with the definition of FIARM staff duties and responsibilities and will provide staff training. In addition, FIARM staff will be assisted and guided in conducting various analysis and reviews. The second component of the project will provide technical assistance to the Sector for Foreign Investments within the Ministry of Economy and other relevant entities involved in the implementation of the national programme for reduction of barriers to investments. This component will focus on improvement of the skills and competences of the staff in developing and implementing programmes for improvement of the administrative and institutional environment for investment. It will also entail drafting of new laws, by-laws and law-amendments related to the investment climate.

3.3.1.2 Small and medium-size enterprise development (approx €2.4 million)

The overall objective of this project is to support the economic growth and improve the business climate in the country through fostering development and performance of SMEs and providing support to key business sectors. The project will entail three components:

- Institutional capacity building for the SME Department within the Ministry of Economy, the Agency for Entrepreneurship Promotion (AEP) and the SME support networks. Technical assistance will be provided to the SME Department and AEP in the implementation of the policy measures derived from the SME Strategy. This component will also aim to integrate various SME support structures and facilitate their co-operation with AEP.
- Non-financial measures to support selected SMEs sectors. This component will include training and consultancy on entrepreneurship, business management and development for the staff of the targeted SME sectors. It will also provide assistance to the Government in the introduction of various financial support programmes for SMEs.
- The third component of the project will work towards the improvement of the dialogue between the public and private sector, in order to increase the participation of businesses in the policy formulation and implementation.

3.3.2 Infrastructure (approx €2 million)

Background and cooperation related policy of Beneficiary country

Since the country's independence, the International Financing Institutions (IFIs) have made available a significant amount of funding to the former Yugoslav Republic of Macedonia in the form of soft loans and grants. Of particular importance are loans provided by the European Bank for Reconstruction and Development (EBRD) and the European Investment Bank (EIB).

European Bank for Reconstruction and Development (EBRD)

The EBRD has been operational in the former Yugoslav Republic of Macedonia since 1993. As of 31 May 2004, the Bank achieved a net cumulative business volume of € 327 million, having signed projects for € 126 million (39% of net cumulative business volume) over the last two years. In June 2004, the EBRD adopted a new strategy for the former Yugoslav Republic of Macedonia. This strategy outlines the priority areas for lending over the following two years, which include private, financial and infrastructure sectors. In the private sector, the EBRD will support foreign direct investments as well as local export-oriented companies through the provision of loans and guarantees. The strategy places a particular emphasis on local companies showing good corporate governance and strong growth potential, and on acquisitions of privatised enterprises by strategic investors. Turn-Around-Management (TAM) and Business Advisory Services (BAS) programs are an integral part of the assistance that will be provided to local enterprises. In the financial sector, the EBRD will seek to enhance financing for SMEs and to further strengthen the banking sector.

The priorities in the infrastructure sector include energy utilities, transport, and municipal infrastructure. In the area of transport, the EBRD will focus on:

- implementation of the Regional Roads Project (Corridor VIII and Corridor X);
- assistance to the authorities in preparing an Institutional Strategy and a Roads Plan;
- co-operation with EIB in the development of a road rehabilitation project combined with sector reform; and
- institutional and structural reorganisation of the Civil Aviation.

The EBRD will also consider financing the modernisation of the Skopje airport and review the most appropriate solution.

The new EBRD strategy emphasises that technical co-operation with other donors and co-financing will be crucial for its implementation. These instruments will also be key to project preparation and institution building, in particular for public sector operations. Moreover, the strategy undertakes "to pursue (EBRD's) operational objectives in close co-operation with the other IFIs active in the former Yugoslav Republic of Macedonia, the European Union and bilateral donors in order to optimise the respective impact of each institution".

European Investment Bank (EIB)

The EIB started its activities in the former Yugoslav Republic of Macedonia in 1998 and to date has provided loans amounting to €163 million. The projects funded by the EIB have mainly focused on road infrastructure, with €130 million provided for construction of sections of Corridor VIII and Corridor X. Remaining projects target small and medium-sized investments by private companies and municipalities and the energy sector. Future EIB plans have been presented in the Medium-term Strategy for the Western Balkans, published in June 2003. This document identifies EIB's strategic priorities for the region, which include further support to the transport, energy and environment sector, as well as possible new areas of funding, including private sector, human capital, health and municipal infrastructure. The strategy also outlines that EIB "remains committed to working in partnership with the Commission, other EU donors and IFIs, to deliver a co-ordinated financing initiative for the benefit of both the individual Western Balkan countries and the region as whole".

The EIB and the EBRD are planning joint interventions in the transport sector, in particular in the areas of air and road transport. However, most of the IFI loans in this sector to date have targeted infrastructure development, as the Government is reluctant to borrow for technical assistance to complement these activities. From an aspect of sustainability of the large infrastructure investments already funded or planned by IFI, it is now crucial to build institutional and legal capacity for their maintenance and management. The Government has recognised this need by requesting technical assistance to the Ministry of Transport and Communications.

Coherence with EC cooperation policy and the MIP

The programme has been specifically designed to address the section of the MIP on co-operation with IFIs.

Specific project interventions, related to the transport sector and compliance of SMEs with environmental standards will address the SAA Articles 57 and 98 on transport, Article 86 on private sector strengthening and Article 103 on prevention of environmental degradation.

Identified projects

3.3.2.1 Co-operation with IFIs – Transport networks management (approx €1 million)

The project will aim to leverage IFI investment in the country through assistance to the Government in improving the management and legal framework for the transport sector. The project has been developed in close co-operation with EBRD and EIB and will seek to complement the joint activities in this sector taking into account the signed MoU on the development of the South-East Europe core regional transport network. Pending further negotiations with EIB/EBRD, the project will focus on one of the following transport areas:

Option 1: Air transport

The project would provide technical assistance in the revision of the air traffic laws and regulations, in particular the Law on Aviation. It would offer suggestions for improvement of the relevant legal acts and would work closely with Ministry of Transport and Communication to facilitate the process of formal adoption of these acts. In addition, the project may revise the relationship between different relevant actors in the air traffic. Or.....

Option 2: Road transport

The project would provide assistance to the Ministry of Transport and Communications and to the Fund for National and Regional Roads (FNRR) with the planning and management of the maintenance of the road network in the country. It would aim to increase the capacity of Ministry and FNRR staff in planning the needs and prioritising the activities in this area. The project would also assist the Fund in the development of an approach for annual planning, resulting in economically sound programmes for road maintenance. In addition, the project may revise the relationship between FNRR and Makedonija Pat in order to create a basis for open competition in road maintenance projects.

3.3.2.2 Co-operation with IFIs – Environmental management (approx €1 million)

The project will support EBRD's Business Advisory Services (BAS) in the former Yugoslav Republic of Macedonia, trying to assist the local SMEs in complying with the new environmental standards. More specifically, the project will provide assistance to the private sector to implement Integrated Pollution Prevention and Control (IPPC) requirements, set out in the new Law on Environment. In this regard, it will support the creation of sufficient local expertise to serve the anticipated demand for skills relating to IPPC and to ISO 14000 Certification. The activities will focus on provision of training to local consultants in developing process descriptions for IPPC permitting and ISO 14000 related subjects. The project will support companies in drafting their compliance plans to the new environmental legislation.

3.3.3 Environment (approx €2 million)

Background and cooperation related policy of Beneficiary country

A fundamental element of the former Yugoslav Republic of Macedonia's accession process relates to harmonisation of its legal framework with the Acquis and to the institutional reforms needed for administration of the new laws. This is particularly important in the area of environmental legislation where a number of new laws have recently been adopted on air, water and waste, but where the capacity for proper enforcement still needs to be built up. The new Law on Waters largely transposes the EU water framework directive and significantly disentangles the existing widely fragmented mandate for water resource management and monitoring, concentrating responsibility in the Ministry of Environment and Physical Planning (MEPP). The new Law on Environment contains key provisions of EU legislation, including the introduction of Environmental Impact Assessment and Integrated Pollution Prevention

Controls. It also provides for the concept of a national Environmental Protection Administration (EPA) with responsibilities for environmental monitoring, at present carried out by a number of entities answering to different Ministries, water management and environmental permitting.

These laws will have a considerable effect in streamlining and strengthening environmental management in the country. That said, a crucial next step is to develop proper institutional arrangements in government to ensure full implementation of the new legislation. In this regard, the MEPP has developed an institutional development plan setting out the implications of the new environmental legislation. The plan takes account of the increased responsibilities of local government in environmental management and their links to the central Ministry. Assistance is now needed in helping the MEPP take forward the new institutional arrangements in government as well as to develop a clear road map for future activities in attaining compliance with the Environmental *Acquis*.

Coherence with EC cooperation policy and the MIP

The project will address the objectives set out in the MIP 2005-2006 for the environment sector, namely, “to support the further alignment of the country’s environmental legislation with EU environmental *Acquis* ”; and “to strengthen Government’s capacity to monitor and enforce environmental standards”. The project will also address the medium-term priorities of the European Partnership in the area of environment as well as reinforce the implementation of the Article 103 of the Stabilisation and Association Agreement. Finally, the project will help reinforce a key principle of the Ohrid Framework Agreement in facilitating the devolution of environmental management responsibilities to the municipal level.

Identified projects

3.3.3.1 Environmental management strengthening (phase III) (approx €2 million)

The project will consolidate the past and current EC interventions in the area of environment management. It will provide further assistance to the legal approximation process and to the development of environmental information system. Key project interventions will include:

- Assistance with the development of a National Strategy for Environmental Approximation. This Strategy will identify the priority areas for legal approximation, will evaluate the costs, and will provide an overall timeframe for implementation.
- A component of the project will specifically focus on compliance of the former Yugoslav Republic of Macedonia legislation with the Air Quality Framework Directive 96/62/EC, its Daughter Directives and other legislation of relevance on air quality protection.
- As a follow-up to phase II of the project funded under CARDS 2004, additional secondary legislation will be developed to support existing laws designed for environmental management and protection.

- The Environmental Information System of the Ministry of Environment and Physical Planning will be further developed through the provision of relevant hardware and software designed to establish real-time interfaces between relevant Ministries and stakeholders.
- Finally, the project will consolidate the institutional development of the Environmental Protection Administration initiated under phase II, with focus on water management related issues.

3.3.4 Education and employment (approx €3 million)

Background and cooperation related policy of Beneficiary country

The former Yugoslav Republic of Macedonia is currently facing a new phase of reform of its higher education system. The priority for the higher education sector is achievement of the objectives of the Bologna Declaration, which aims for a common higher education space in Europe by 2010. The former Yugoslav Republic of Macedonia signed the Bologna Declaration in September 2003. This was an important step-forward with participation in the Bologna process, requiring realisation of a number of key reforms. These include structural reforms of university governance, management and finance of universities; efficient control over standards; and the setting up of a system to test compatibility across faculties and universities.

With the recognition of Tetovo University in 2003, there are now three state universities in the country – “Sv. Kiril i Metodj” in Skopje, “Sv. Kliment Ohridski” in Bitola and Tetovo University. Moreover, there are a number of private universities, prominent of which is the multilingual South East Europe University in Tetovo. The reforms that underpin the Bologna Declaration will be instrumental for these universities’ future development and integration into the European higher education system.

Coherence with EC cooperation policy and the MIP

The programme for higher education (TEMPUS) directly address objectives set out in the MIP 2005-2006. TEMPUS also directly addresses Article 91 of the SAA, on co-operation in the area on education and training. Both components reinforce priorities of the European Partnership.

Identified projects

3.3.4.1 TEMPUS : Multilateral co-operation for the development and restructuring of higher education (approx €3 million) (COMMISSION MANAGED)

The project will aim to support the country’s efforts to achieve the objectives of the Bologna Declaration which aims at the establishment of a common European higher education space by 2010. The project activities will be implemented through three instruments: Joint European Projects; Structural and Complementary Measures; and Individual Mobility Grants and will focus on:

- increased synergy between higher education legislation and policy and reforms at the institutional level;
- strengthened strategic management capacities of higher education institutions;
- modernisation of management and administration of the participating higher education institutions;
- teaching and learning according to revised curricula and study courses in line with changes of social and economic needs;
- improved skills of non-academic staff relevant for public administration reform and civil society development;
- increased mobility of students and academic staff; and
- closer co-operation and sharing of resources and experience between higher education institutions at a regional level.

3.4 General Technical Assistance Facility and Programme Reserve (approx. €1.4 million)

The main purpose of the General Technical Assistance Facility (GTAF) (€1 million) is to allow project preparation to proceed in a quick and effective manner. The GTAF will support the preparation and early implementation of activities under the Annual Programme, and support the planning process for future Programmes. Actions to be supported are likely to include: (i) recruitment of short-term technical assistance (local and international) for activities typically including feasibility studies, inputs to terms of reference and specifications, and tender evaluations; (ii) audits, monitoring, thematic / programme / project evaluations; and (iii) project preparatory and start-up actions.

The former Yugoslav Republic of Macedonia 2005 Programme Reserve (€0.4 million) will be used to cover additional programme related expenditures that are currently unforeseeable. This arrangement is particularly important for maintaining a flexible capacity to respond to significant issues that might arise on existing projects or to other unforeseen developments where assistance had not previously been targeted.

3.5 Community programmes (approx. €2 million)

At the Thessaloniki Summit in June 2003, the EU agreed to open participation in Community programmes to the Western Balkan countries, following the approach used in the candidate countries. A framework agreement with the European Community laying down the general conditions for the participation of the former Yugoslav Republic of Macedonia in Community programmes will be concluded and is expected to enter into force early 2005.

The objective of the Community programmes is to support the country's efforts towards European integration by facilitating transfer of know-how and good practice, particularly in those areas of the Acquis that serve as key reference points for its reform process. It will also help the country and its citizens to familiarise themselves with the Union's policies and working methods.

The Community programmes are EU internal action programmes and therefore partner countries outside the Union must pay a financial contribution ('entry ticket') to cover the expenses of participation in specific programmes. For a given programme, this 'entry ticket' will be determined in a corresponding Memorandum of Understanding (MoU) between the country and the Commission.

As participation in Community programmes can represent a large investment for a partner country, CARDS support may be used to co-finance 'entry tickets'. In the case of the former Yugoslav Republic of Macedonia an amount of €2 million has been made available for this purpose in 2005. As a number of Community programmes require the existence of a substantial administrative structure to allow a country's full participation, these funds may also be used for accompanying measures such as capacity building to implement specific programmes or training of potential participants.

4. Past EC assistance and lessons learnt

Past EC Assistance

Between 1992-2004, the EC committed some €736 million to the former Yugoslav Republic of Macedonia. This figure includes development programmes funded under Phare, Obnova and CARDS, contributions to emergency humanitarian relief and for balance of payments support.

Humanitarian aid (through ECHO)	€106 million
Phare / Obnova / CARDS assistance	€409 million ⁽⁸⁾
Rapid Reaction Mechanism (2 programmes) and Special CARDS Emergency Programme	€26 million
Macro-financial assistance	€138 million
Other forms of financial support, e.g. subsidies	€65 million
	€736 million

The European Agency for Reconstruction is managing inherited and recent EC assistance programmes in the former Yugoslav Republic of Macedonia, including programmes under Phare, Obnova and CARDS. The table below summarises progress on the implementation of previous EC programmes, managed by EAR, dating back to 1997:

	Funds committed	Contracted (% of committed)	Paid (% of committed)
Phare COP, CBC 1997	€8,615,809	100%	96%
Phare COP, CBC 1998	€21,889,545	100%	100%
Phare COP, CBC 1999	€21,200,690	100%	79%

⁸ Includes cumulative programme funds now managed by the European Agency for Reconstruction and also those being managed directly by the European Commission (customs and taxation; Tempus higher education programme), and the Agency's cumulative administrative expenditures.

Phare COP 2000, National Programme 2000, Obnova 2000	€18,028,907	100%	81%
Rapid Reaction Mechanism 1 and 2 and CARDS Emergency Programme 2001	€25,831,395	100%	100%
Action Programme 2001	€31,071,106	100%	58%
Action Programme 2002	€33,500,000	88%	51%
Action Programme 2003	€33,500,000	66%	17%
Action Programme 2004	€51,000,000	37%	(yet to be disbursed)

Lessons Learnt

Some of the more important lessons learned from EC and other donor programmes in the former Yugoslav Republic of Macedonia and applied to the 2005 programme are the following:

- Low absorption capacity is the single biggest constraint to programme planning and implementation in the former Yugoslav Republic of Macedonia. Such constraints also reduce the propensity for local ownership and sustainability of projects. Ministries within the Government are often overwhelmed with technical assistance offered by various donors. This is particularly the case in the Ministry of Economy and the Ministry of Interior. It is therefore essential that any programme of technical assistance results from a thorough analysis of what the relevant Ministry or government agency can take on at that point. The development of the 2005 programme began in early 2004 so as to allow the necessary time for design studies, proper appraisal of viability, risk and sustainability issues. The different sector programmes are the result of an ongoing dialogue with key Ministries and in many cases interventions flow from early activities under CARDS.
- A major pillar of the 2005 programme is implementation of the Ohrid Framework Agreement. Wherever possible the principles of the Framework Agreement – decentralisation, non-discrimination, equitable representation, use of languages – have been mainstreamed throughout the sector programmes rather than targeted in stand-alone projects where impact is questionable. So, for example, decentralisation and strengthening of municipalities underpins activities in the economic development and environment sectors as well as, of course, in the public administration reform programme. Similarly, issues of equitable representation are not only addressed in the projects proposed under democratic stabilisation but underpin interventions in the sectors of justice and home affairs, education and employment.
- One area which is generally viewed as critical to any future stability and development of the former Yugoslav Republic of Macedonia is the rule of law. There is a general consensus – acknowledged by the Government itself – that one of the most critical barriers to the country's economic development and realisation of reforms is the weak rule of law. With this in mind, there is an increased emphasis within the 2005 annual programme on strengthening the rule of law across all sectors. There are programmes aimed at generally building up the prosecutorial system whilst other

interventions address the capacity of the public service to deal with corruption and financial crime, including money laundering. These interventions reinforce the broader police and justice reform strategies, as well as the reforms in the customs service, all of which are either being developed or under implementation with CARDS assistance.

- A final development in the 2005 programme which draws on past experience is the still very weak enforcement capacity of government. Despite progress in legal harmonisation and approximation to the EU Acquis, compliance with the principles and provisions of the new laws is often, at best, variable. There is a real need to strengthen the capacity of relevant government departments to implement and monitor enforcement of new legislation. Again, this need is reflected in the 2005 programme where the emphasis is less on harmonisation of further legislation and more on consolidating progress in relation to already adopted laws. In this vein, institutional strengthening is planned for key ministries involved in enforcement of new laws, for example, the implementation of the new Trade Laws under the Ministry of Economy.

Complementary actions

The proposed 2005 Action Programme for the former Yugoslav Republic of Macedonia extends the initiatives and builds on the achievements of previous EC assistance. A significant proportion of CARDS assistance is focused on institutional building projects, which, by their nature, often require a long period of time to demonstrate results. It has therefore been important to ensure that EC programmes adopt a phased approach in certain sectors such as police and fight against crime, environment and employment. The 2005 programmes in the above sectors are a continuation of activities, complementing and enhancing interventions under earlier CARDS programmes.

In other sectors, the minority rights programme has a clear read-across to the Commission-managed European Initiative for Democracy and Human Rights (EIDHR) and past ECHO projects in this area. Similarly, the proposed programme for employment draws on the regional experience of the European Training Foundation (ETF). In the area of JHA, the CARDS programme on police reform reinforces the work of the EU Police Mission (Proxima) currently operating in the country.

The 2005 programme also seeks to complement the assistance made available to the former Yugoslav Republic of Macedonia under other EC programmes and instruments. New assistance instruments were introduced following the Thessaloniki Summit in 2003, in particular the New Neighbourhood Programme and Community Programmes. It is important that the national CARDS programme enables the advancement of these new instruments. Moreover, in view of the importance of regional co-operation for the development of the country, the national CARDS programme aims to complement Regional CARDS activities; this is particularly the case in the JHA sector.

Donor coordination

A close dialogue with the key multilateral and bilateral donors in the former Yugoslav Republic of Macedonia was maintained during the development of the programme. Co-ordination has been on going at both project design level and at a policy level. Of particular importance were the co-ordination activates with the IFIs, including the World Bank, EBRD and EIB. To synchronise future policies and maximise the impact of the programmes, the EC and World Bank have had an ongoing dialogue both in Skopje and Brussels. A number of meetings with EBRD and EIB have also taken place, resulting in the development of joint programmes in the areas of transport and environment.

Throughout the design and implementation of EC programmes, the Agency closely liaises with the EU Member States' representatives in-country. The monthly meetings with Member States, chaired by EAR, have served as a valuable forum for co-ordination of activities and exchange of information. Such co-ordination efforts have been of particular importance in reinforcing different programmes across a number sectors, notably in the donor-congested areas of decentralisation and municipal development. To facilitate the co-ordination process, EAR has recently produced a donor matrix outlining all Member States' bilateral programmes across MIP sectors. The matrix shows what the whole EU family is contributing to the former Yugoslav Republic of Macedonia.

Consultations with USAID, the most significant non-EU bilateral donor, have also been crucial, particularly in the areas of business development and justice. Moreover, it was also important that the proposed JHA programme was co-ordinated with the activities of OSCE and the Council of Europe.

Cost and financing

The Programme will be financed through a Community grant of €34.5 million, allocated among the following sectors:

Priority sector	€ million (+/- 20%) ⁽⁹⁾
Democratic stabilisation	
1.1 Minority rights	2.0
Good governance and institution building	
2.1 Justice and home affairs	3.5
2.2 Public administration reform (including Commission managed projects: Customs - approx €3 million and Decentralisation of management of assistance - €1.3 million)	15.0
Economic and social development	
3.1 Investment climate	3.6

⁹ Individual financial allocations are subject to fluctuations of up to ± 20% over the programme's lifetime.

3.2 Infrastructure - Co-operation with IFIs	2.0
3.3 Environment	2.0
3.4 Education and Employment (Commission managed Tempus project, approx €3 million)	3.0
General Technical Assistance Facility and Programme Reserve	
4.1 General Technical Assistance Facility and Programme Reserve	1.4
Community Programmes	
5.1 Participation of the former Yugoslav Republic of Macedonia in Community Programmes	2.0
TOTAL	€34.5 million ⁽¹⁰⁾

The Programme will be implemented by the European Agency for Reconstruction, except for actions in the area of customs, higher education (Tempus), decentralisation of management of assistance and Community Programmes, which will be managed directly by the European Commission.

¹⁰ Excludes the Agency's 2005 administrative appropriations for managing the cumulative portfolio of EC assistance to the former Yugoslav Republic of Macedonia, which are the subject of a separate 2005 financing proposal.