

ANNUAL ACTION PROGRAMME 2003 FOR SERBIA

1. IDENTIFICATION

Form of programme:	“National programme”
Beneficiary Country:	Serbia and Montenegro/ Republic of SERBIA¹
Budget Year:	2003
Financial Allocation:	€229 million
Budget lines:	B7- 542
Legal Basis:	Council Regulation (EC) No. 2666/2000 (as amended by Council regulation (EC) No. 2415/2001)
Contracting:	All contracts must be concluded after the signature of the Financing Agreement and within 36 months following the date of the budgetary commitment.
Implementation:	The implementation of projects under this proposal must be concluded by 31.12.2007. Therefore, all technical activities provided for under this programme and all contracts must end by 31.12.2007.
Implementing Bodies:	European Agency for Reconstruction - €220 million European Commission - €5 million for Customs & Taxation; and €4 million for Tempus
Remarks:	No administrative expenditure will be financed under this programme.

2. SUMMARY OF THE PROGRAMME

The proposed Annual Action Programme will provide assistance for key aspects of the country's economic and social reform agenda and especially for the state of Serbia and Montenegro's rapprochement toward European structures, in line with the Stabilisation and Association process. In particular, this Annual Programme reflects the Commission's Country Strategy Paper (CSP) for FRY and the associated three-year (2002-4) Multi-annual Indicative (MIP) programme. In line with the Consultative Task Force (CTF) and Stabilisation and Association process discussions, increased emphasis and resources have been placed on "Good Governance and Institution Building" programmes. The overall programme will be implemented in close coordination with programmes of other donors, particularly those of the EU Member States, and also in complementarity with the CARDS Regional programme and other

¹ Since the name of the State only changed in February 2003, the term FRY is maintained in references to earlier official documents.

CARDS assistance programmes in Serbia and Montenegro. The priority sectors in the Annual Programme are as follows:

Sectors (<i>titles as per MIP</i>)	€ millions (+/- 20%)²
1. Good Governance and Institution Building	
1.1 Public Administration Reform – General	2.0
1.2 Public Finance Management	20.0
1.3 European Integration/New Union Structures	9.0
1.4 Justice and Home Affairs	13.0
1.5 Customs and Taxation (Commission managed)	5.0
1.6 Public Administration Reform – Health	9.5
2. Economic Reconstruction, Regeneration and Reform	
2.1 Energy	69.0
2.2 Transport	4.5
2.3 Environment	12.5
<i>Economic Development</i>	
2.4 Rural Economy/Agriculture	7.0
2.5 Privatisation and Enterprise Development	13.5
2.6 Local/Municipal Development	35.0
3. Social Development and Civil Society	
3.1 Vocational Education and Training (VET)	13.0
3.2 Civil Society	1.0
3.3 Media	6.0
3.4 Tempus (Commission managed)	4.0
4. Other	
4.1 General Technical Assistance Facility (GTAF) & Programme Reserve	5.0
TOTAL	€229 million³

² Individual financial allocations are subject to fluctuations of up to +/- 20% over the annual programme's lifetime.

³ Excludes the Agency's 2003 administrative appropriations of approx. €11 million for managing the cumulative portfolio of EC/EAR assistance to Serbia and Montenegro /Republic of Serbia. The Agency appropriations are the subject of a separate 2003 Financing Proposal on Administrative Expenditure.

3. Country Background

Political

Political debate over the last year has centred on the redefinition of the constitutional framework of the FRY. The republican as well as the federal parliaments have now ratified the Belgrade Agreement of March 2002 and the process of translating the principles embodied in the Agreement into operational arrangements has been underway since June.

Domestically, the Serbian Government also faces the need for constitutional restructuring, with demands for further autonomy from the provincial government in the northern province of Vojvodina. Relations with Kosovo continue to evolve and a dialogue between the United Nations Interim Administration in Kosovo (UNMIK) and Belgrade authorities on a number of topics has been initiated. Although political uncertainties (and party positioning) over the past year have occupied the attention of policy makers, these have not derailed the economic reform effort. While reformist political leaders remain popular (despite Serbia's recent inability to elect a new President), maintaining widespread support for continuing reform efforts is likely to be a key challenge throughout the remaining period of the MIP (up to end of 2004).

Regional stability and cooperation within South Eastern Europe have greatly improved. On-going efforts by the international community to consolidate stability in the region – especially a clear path to European integration through the EU's Stabilisation and Association process – have provided strong incentives for reform and cooperation. At the same time, the democratic transition in Serbia and Montenegro has also greatly contributed to improved relationships within the region; some acceleration in the return of refugees and the on-going process of regional trade liberalisation are tangible results. These developments should reduce the risk that current domestic political challenges could lead to backtracking on economic and political liberalisation.

The international community continues to ask Serbia and Montenegro authorities to act on security related issues, improve their cooperation with the Hague Tribunal, implement the new constitutional charter, and follow the actions planned for achieving the harmonisation of the state's internal market.

Economic

Since late-2000, the key policy instrument for restoration of macroeconomic stability was a renewed focus on adjusting fiscal deficits towards levels that can be financed from non-inflationary sources. At the Federal and Serbian levels, it was motivated by the need to confront and manage the growing hidden fiscal liabilities that grew out of the unsustainable policies of the past.

These tighter macroeconomic policies were first supported by an IMF Emergency Post-conflict Facility approved in December 2000, followed by an IMF Stand By Arrangement approved in June 2001 and a three year IMF Extended Arrangement for \$825 million in May 2002. Successful implementation of these programmes has brought visible progress while laying the foundations for a more sustained recovery and improved living standards. Estimates for end 2002 inflation are about 15% with a

continuing downward spiral for 2003. Commercial interest rates continue to decrease. The nominal exchange rate of the YUM to the Euro has remained stable since December 2000. Subsequent real appreciation of the currency primarily reflects adjustment from an initially undervalued level. Exchange rate unification and liberalisation of the foreign exchange market has brought about current account convertibility. FRY's official foreign reserves grew to US\$2.1 billion by September 2002 (more than five months of imports), easily exceeding targets under the IMF programme.

GDP growth rebounded from the highly negative rate of 1999 (influenced by the Kosovo conflict) to about 5.5% in 2001 and may reach 4% in 2002. Industrial activity, (33% of GDP) with substantial potential for growth, has remained flat over the past two years. Resumption of enterprise growth will require on-going structural reforms in the real sector of the economy as well as further development and strengthening of the financial and banking sector. The 2001 fiscal deficit of 1.4% of GDP (relative to an expected deficit of 6.3%) was achieved through revenue over-performance of about 1% of GDP accompanied by expenditure compression of almost 4% of GDP. Projections for 2002 show a fiscal deficit of about 5.0%, which is expected to be largely funded by foreign loans, grants and privatisation receipts. Per capita GDP is now (2002) estimated at US\$1,130. Reductions in quasi-fiscal deficits (e.g. through higher energy prices, which helped to contain the losses of state-owned power companies) and a highly concessional November 2001 debt restructuring agreement with the Paris Club further enhance prospects for medium term sustainability.

OECD's recent economic report concluded that a solid foundation had been laid, though real economic growth will remain a challenge, and that the momentum for change must be maintained so as to complete the transition to a free market economy.

4. PAST EC AND OTHER DONORS' ASSISTANCE

Between 1998-2002, the EC committed some €1,117⁴ million to Serbia and Montenegro (excluding Kosovo). These funds were used for emergency and humanitarian relief, developmental activities and for balance of payments support.

- Humanitarian (ECHO)⁵ €211 million
- CARDS (EC/EAR), OBNOVA €561 million
- Macro Financial (balance of payments support)³ €345 million

⁴ All figures are rounded to the nearest € million.

⁵ECHO figures are from 1999-2002 and are for Serbia programmes only.

³ The Council, on 5 November 2002, adopted a Decision providing further Community macro-financial assistance to the FRY in the amount up to €130 million

Other active donors (commitments) since 2001 were most EU Member States (about €350+ million in bilateral aid), USAID (about \$150+ million), Switzerland, Norway and Japan. In particular the IFIs, especially the IMF, World Bank, EBRD and the EIB, have developed large programmes of over €1.5 billion to be executed over the next few years. Last but not least, many of the UN family organisations were also active e.g. UNDP, UNHCR, UNESCO, WHO, FAO, ILO and UNEP.

According to the Ministry for International Economic Relations (MIER), Serbia and Montenegro /Republic of Serbia (excluding Kosovo) received over €2.7 billion in donor commitments between 2000 and July 2002.

As of 2 December 2002, the global rate of contracting for combined 1998-2001 programme funds was 99% of commitments, with the payment rate corresponding to 89% of commitments; while the corresponding percentage rates for the 2002 programme funds are 82% contracted and 21% paid.

5. PROGRAMMING CONTEXT, IMPACT AND LESSONS LEARNT

Programming Context

The FRY Country Strategy Paper (CSP) identified a series of problems that Serbia needs to address, such as enhancing the efficiency of the state, promoting economic growth developing human capital and in particular respecting processes (e.g. CTF/SAP), which allow a rapprochement with European norms and structures.

An anticipated and recommended funding shift from emergency to economic development has already taken place with the 2002 programme. In the 2003 programme a further gradual funding shift is taking place from economic development to the good governance/institution building sectors. It also places greater emphasis on coordination and harmonisation with similar sectoral programmes in Montenegro (e.g., Justice and Home Affairs; food chain safety systems) to foster Union harmonisation.

The proposed Annual Action Programme outlined below reflects this philosophy and the Multi-annual Indicative Programme (MIP).

Impact of Previous Programmes

Energy: A 15.2 % year-on-year increase in electricity output between 2001 and 2002; systems reliability increased by 6% and forced outages reduced by 8%; a 70% increase in overburden removal at coal mines and 16% increase in coal production in 2002, compared with 2001.

Health: In the first half of 2001 the serious shortages of drugs in hospitals and state pharmacies were alleviated as a result of the 2000 emergency supply project

Municipal development: Through the "Towns and Schools for Democracy" programme 137 municipalities benefited from school rehabilitation works; 88 from water supplies and sanitation works; 120 have received supplies of school furniture, computers, garbage containers/trucks or other special vehicles. All 160 municipalities

benefited from at least one component. It was a well-received programme with high visibility.

Enterprise development: Approximately 700 jobs have been created through the credit lines for SMEs; hundreds of Serbian entrepreneurs and enterprises were supported through information, advisory and training services; EC funded credit lines also served as a catalyst for other donor funded credit lines (EIB, €20m) and assisted in establishing more market based (competitive) interest rates, which resulted in a considerable reduction in interest rates from an average of 2.2% to 1.2% per month.

Rural economy: a new agricultural laboratory network has been designed, establishing national reference laboratories based on EU norms and standards for agricultural products; in South Serbia (Presevo) 2260 workers were employed for about 12 months contributing to a noticeable increase in social stability.

Lessons Learnt

The most *important lessons learned* may be summarised as follows: (i) ensure institutional absorptive capacity, sufficient counterparts and budget allocations; (ii) project contract specifications need to better reflect risk management measures; (iii) ensure full understanding of implications by project partners of project related conditionality; (iv) donor coordination is a continuous process; and (v) programming and related project preparation (e.g., feasibility studies) and coordination need to begin as early as possible. These lessons are reflected in the design of the 2003 programme.

Finally, agreement needs to be reached on the annual action programme by all concerned parties (including on documentation standards) before mid-year.

6. Programme Components and Project Activities – Serbia and Montenegro / Republic of SERBIA 2003

A description follows for each programme component to be assisted, preceded in each case by a background justification for the selection of the various project activities within each programme component and a summary of related EC assistance and other donor activities. Further details (including log frames) of individual projects are to be found in a separate set of Project Annexes – having working document status.

6.1 GOOD GOVERNANCE AND INSTITUTION BUILDING (approx. €58.5 million)

This section will propose programmes in more general public administration reform, public finance management reform, support for European integration, justice and home affairs, customs and taxation, as well as institutional reforms in the health sector:

6.1.1 General Public Administration Reform, Public Finance Management and Support for European Integration (approx. €31 million)

Background

The *overall public administration reform* programme of the Republican government is oriented towards building the capacity of public authorities (including the setting-up of an appropriate institutional and legal framework) so that these are in a position to (i) deliver their services in an efficient, effective and accountable fashion, and (ii) redress a working culture dominated by bureaucratic rather than service-oriented requirements.

A new Law on Ministries (24 May 2002) substantially changed the structure of the Government of Serbia. This law reorganised the institutional responsibility for the reform of the public administration by creating a new Ministry of State Administration and Local Self-Government (MSA/LSG). In principle, the creation of the new Ministry has put under one umbrella a number of competencies that were spread among different ministerial and government agencies. However, in practical terms, the areas of influence remain rather undefined and the transition is far from complete. It will need to overcome three main impediments: (i) weak institutional capacity, (ii) lack of professional expertise, and (iii) lack of public awareness on the Ministerial activities.

Public finance reforms are another key component for success of overall public administration reform. These reforms will ultimately lead to a Serbian Ministry of Finance and Economy (MoFE) that co-ordinates and controls the state budget preparation and execution (in particular the treasury function) and ensures government internal financial control (increased efficiency and effectiveness of public finance). They will also improve the parliamentary oversight of the state finance system by (among other measures) establishing a Supreme Audit Institution based on EU best practice (reinforced accountability and transparency).

Further reforms will strengthen the tax administration, a system of public internal financial controls and the closure of the Central Agency for Payment and Settlement (known as ZOP). The Public Revenue Agency resulting from the closure of the ZOP lacks modern systems, equipment and training to maintain and improve the current rate of tax collection and to introduce new taxes such as the Value Added Tax (foreseen for January 2004). Internal financial controls remain inefficient and cannot ensure a proper control of budget execution. There is also no independent public body such as a Supreme Audit Institution to ensure the financial accountability and transparency. With its current bureaucratic processes and poor computerisation, the MoFE is unable to efficiently co-ordinate and control state budget preparation and execution. New systems and processes will be implemented for this purpose.

European Integration: In order to meet the immediate objectives of WTO membership, and with the perspective of EU integration through the Stabilisation and Association process, the state union of Serbia and Montenegro is required to develop a common trade policy and take measures in order to adopt a single external tariff, eliminate trade barriers and gradually achieve conformity with EU technical regulations and European standards. Serbia and Montenegro has chosen to follow a EU compatible path from the outset, committing itself to promote technical harmonisation and foster the development of national Quality Infrastructures

(standardisation, certification, accreditation, metrology) able to drive the process of trade liberalisation. The restructuring of the state and the redistribution of certain competences makes the rationalisation of quality infrastructures between the two Republics and the adoption of a single national policy in line with EU principles, even more critical.

In this context, the EC will also assist with the establishment of systems and structures *to help consolidate the new Union* as well as provide resources to conduct conferences/workshops aimed at domestic opinion formers and decision makers in order to have public debates on key policy issues related to EC core assistance programmes and raise the general awareness of EU integration issues.

Complementary and Past EC Assistance

The EC has launched a number of technical assistance initiatives such as: creation of a national Treasury and a Public Procurement Agency; strengthening the tax administration and some initial steps towards establishing a system of public internal financial control and a Supreme Audit Institution; supporting the transition of the fiscal administration from ZOP to the Public Revenue Agency; and defining strategies for institutionalisation of the Ministry (MSA/LSG). These served as the basis for the development of the proposed 2003 overall public administration/finance programme activities. In addition, there is a close linkage of this programme with the proposed EC 2003 Local/Municipal Development Programme, especially concerning the development of a regional policy. The EU also supports quality infrastructures development through the EC CARDS regional project "Trade related technical assignments: Quality Infrastructure". That project aims to ensure appropriate conditions for joint projects between CARDS countries' "Infrastructures" institutions by promoting coordination mechanisms.

Related Activities of Other Donors

An increasing number of bilateral and multilateral co-operation projects are targeting the two Ministries, Finance and State Administration, and the State agencies active in Public Administration reform. Worth mentioning is the UNDP "Capacity Building Fund" project, which will support most of the principal institutions, and also a large human resource reorganisation project launched by SIDA with the Government Agency for Public Administration Development; GTZ assistance for Value Added Tax; related French and US Treasury actions. The preparatory analysis for public internal financial control and audit was carried out jointly by SIDA and the Agency. France also provided support to the Public Revenue Agency.

Project Activities

6.1.1.1 Strengthening the Ministry of State Administration and Local Self Government - MSA/LSG (approx. €2 million)

Experts will essentially assist in the reorganisation and operations of the State Administration sector in line with EU/CoE standards of public management, including creating a Training Centre for Middle Management in the Ministry, which will provide theoretical and on-job-training schemes to middle management civil servants (assistance will also be provided for the initial running of the Centre). The proposed

project will also provide a limited amount of project related equipment for the Ministry, especially for the Training Centre.

The Ministry of State Administration and Local Self Government (MSA/LSG) will work closely with the Project Implementation Unit and formal Working Groups as well as ensure availability of sufficient human and financial resources and working facilities for the Contractor.

6.1.1.2. Support to Public Finance Reforms (approx. €20 million)

Experts will essentially review the organisation, propose improvements, prepare operational manuals and assist in the procurement of IT equipment and related training for the *Public Revenue Agency, MOFE, and Supreme Audit Institution*. These activities will ultimately lead to a Serbian Ministry of Finance and Economy (MoFE) that is able to (i) co-ordinate and control the state budget preparation and execution (in particular the treasury function); (ii) ensure Government internal financial control (increased efficiency and effectiveness of public finance); and (iii) improve parliamentary oversight of the state finance system by (among other measures) establishing a Supreme Audit Institution based on EU best practice (reinforced accountability and transparency).

The project partners (MoFE and for the Supreme Audit Institution Parliament & MoFE) will (i) appoint a senior member of staff to liaise with the respective contractors, (ii) ensure that sufficient human and financial resources are available, (iii) ensure that working facilities are available for the contractors, (iv) facilitate the implementation of the foreseen Advisory Boards and Steering Committees. Project partners will also sign a Memorandum of Understanding specifying each partner's implementation responsibility.

6.1.1.3 European Integration / Union of Serbia and Montenegro structures (approx. 9 million)

Experts will (i) ensure a gradual transposition of EU technical regulations and adoption of European standards (ii) design and deliver training (quality infrastructures) to staff from concerned Ministries, (iii) support the implementation of a quality plan for related industry sectors. This support will be provided to the following institutions: *Federal Office for Standardisation (SZS), Yugoslav Accreditation body (JUAT), Federal Bureau of Measures and Precious Metals (FBMPM)*. Such support will also be given to the *conformity assessment bodies*.

New Union/Federal Structures: Experts will also support activities related to new Union/Federal structures, once these have been defined. For example, such activities could assist in: an extension of the scope of the Policy and Legal Advice and Coordination Unit (PLAC/SCEPP); expanding the support to European Integration Units at the Republican levels; etc.

EU Integration Conferences/Workshops: An expert or a specialised institution will administer a fund on behalf of Government to (i) develop selection criteria and appraise requests for the support of workshops, seminars, cultural activities, dissemination of information, etc.; (ii) prepare annual work plans under the direction of a joint Agency/Government Steering Committee; (iii) assist with publication of

supplements, brochures, pamphlets and other forms of information dissemination; and (iv) fund participation of state representatives in conferences / workshops essentially related to EU integration and regional cooperation.

Project Partners (relevant Ministries, SZS, JUAT, FBMPM) will (i) appoint a senior member of staff to liaise with the respective contractors, (ii) ensure that sufficient human and financial resources are available, (iii) provide working facilities for the contractors, (iv) facilitate the implementation of the foreseen Steering Committee.

6.1.2 Justice and Home Affairs (approx. €13 million)

Background

Of particular concern for Serbia and Montenegro, neighbouring countries and the international donor community is the field of Justice and Home Affairs (JHA). Serbia, with its unique geo-political position, is facing an increase in local and regional crime, much of it cross-border in nature and international in dimension.

There is a growing consensus on the need to take swift and effective action. The objectives of this action would be not only to bolster existing law enforcement agencies, but also to ensure that they operate in an EU compatible framework (both in terms of legislation and work processes); it would then improve the institutional capacities of the local services as they take on an increasing share of operational responsibilities. Numerous initiatives have been launched to tackle the regional consequences of organised and cross-border crime in Serbia, including activities under the Stability Pact, the SAP and the CARDS programme, as well as bilateral assistance programmes. The recent JHA EU experts' mission to Serbia and Montenegro has also confirmed the need to strengthen border management and anti-organised crime bodies as part of a combined approach to combating organised and cross-border criminality and to meeting the need to strengthen local capabilities of law enforcement bodies generally. The proposed programme is based upon these recommendations and reflects a coordinated approach with Montenegro and Kosovo. In the implementation phase, the respective programmes will be jointly coordinated to ensure similar strategies, policies and systems applied within the entities.

Complementary and Past EC Assistance

The police project has been devised to improve border management and control systems, so that there are harmonised border controls (based on the Schengen acquis) throughout the state. The projects will be closely coordinated with other ongoing initiatives, such as the CARDS regional JHA and IBM programmes, the CAFAO-FRY, the activities of the Stability Pact (its 'Table 3') and other initiatives such as the Council of Europe's activities in the legislative field. Further support to the Ministry of Justice will build on the on-going 2002 programme, which focuses on efficiency improvements to court management systems.

Related Activities of Other Donors

The proposed activities will complement ad hoc JHA assistance already provided by other multilateral and bilateral donors, e.g. DFID, GTZ, Norway, and Canada. In particular, significant cooperation is foreseen with OSCE, which has conducted many

assessments in the areas of JHA in Serbia and Montenegro at state union and entity level.

Project Activities

6.1.2.1 Justice and Home Affairs / Support to the Law Enforcement Agencies and to the Justice System (approx. €13million)

EC assistance will essentially be used for the definition of EU compatible strategies/policies/guidelines, work processes, information flows and techniques supported by the provision of appropriate equipment and related training for the *Border Police, Criminal Police (Belgrade), Prosecution Service, and for the Ministry of Interior's Information and Communications Department and Organised Crime Directorate*. The design of the project is being coordinated at state level with a CARDS project at Serbia and Montenegro /Republic of Montenegro level, and a similar project in UN administered Kosovo.

The Ministry of Justice will also receive further expert support (building on the current project) with the aim to (i) define an overall reform strategy and priority intervention areas and (ii) introduce alternative (out of court) conflict resolution mechanisms such as mediation or arbitration.

A Programme Management Unit (PMU) will be set up with EU experts to supervise project implementation. The major implementation partner for IT will be the Ministry of Interior's Information and Communications Technology (ICT) Department. The Serbian Border Police and Agency-assigned experts will collaborate in the specification of other border management equipment, and work together with the ICT and the relevant contractors assigned to this task. In addition, each beneficiary must demonstrate adequate absorption capacity in relation to the enhancements provided under this project and subsequent implementation phases. Also, funds will be provided for maintenance.

6.1.3 Customs and Taxation (approx. €5 million) - Commission managed

Background

Since the signing of the Belgrade Agreement, customs has become increasingly important because of the requirement that there be a single market and a single economic space within the territory of the state.

The customs and taxation authorities are in the process of implementing comprehensive programmes of modernisation and development in order to improve revenue collection, to support the fight against fraud and corruption and to facilitate legitimate trade. This project will provide continued assistance to the authorities and ensure that the modernisation is based on EU best practice in the fields concerned.

The assistance will focus on supporting managers of the customs and taxation services in the implementation of a long-term modernisation and development strategy. It aims to achieve a cohesive management of the customs and taxation functions, with a view to promoting the concept of a single economic space within the State, along the model of the EU single market

Project Activities

6.1.3.1 Support to Customs and Taxation (approx. €5 million)

EC funds will target not only *customs* activities supporting the state level in its efforts to restore a single economic space and a single market, but will also support the Republics, which will be responsible for the implementation of the state-level policy.

This is a continuing programme, which aims to assist local authorities to complete a comprehensive modernisation and development of the customs area, based on the EU Blueprints, and notably to support the implementation of the undertaking, in the Belgrade Agreement, to create a single market and a single economic space. Activity in 2003 will provide continuing assistance in many of the Blueprint areas.

The *taxation* authorities are receiving substantial assistance in the areas of both direct and indirect taxation (except excise) from other donors (e.g. US Treasury and Germany - GTZ). This project will thus, when required, focus on ensuring efficient co-ordination between the customs and taxation authorities particularly in respect of VAT collected at importation and in the development of modern and effective excise regimes.

6.1.4 Public Administration – Health (approx. €9.5 million)

Background

The Government of Serbia considers the reform of the health sector as a national priority. Several positive steps have been taken so far, such as the establishment of a National Health Council (in December 2001) and an expert advisory board, and also a Health Care Reform Commission (HCRC) in July 2001. Leading the consultative process on behalf of the Ministry, the HCRC has developed a framework for national health policy in Serbia, which was adopted by the Government in February 2002. This document has many excellent components, but remains unsatisfactory because it does not fully integrate policies and implementation strategies.

Lack of clarity on the division of responsibilities between the main stakeholders has hindered the health sector reform process so far. Work relationships between the Republican Ministry of Health (MoH), the state level Health Secretariat, the Republican Health Insurance Fund and the Republican Institute of Public Health are unclear and inadequate for an effective health management system. An EC funded assessment mission has confirmed that the MoH needs urgent support and technical assistance in building its capacity to fulfil its mandate and responsibilities.

Health infrastructure, including curative and preventive services, has gradually deteriorated in Serbia over the last ten years. The country is now facing difficulties in financing even the basic services due to a poorly functioning contribution system and lack of clarity on the division of responsibilities between the main players. Disease prevention, though historically considered as the flagship of any national health system, remains under-funded. Also, no clear vision exists as to what kind of

preventive services should be included in a basic package of health services, which results from a lack of a strategy to address public health problems.

Lack of strategic leadership has also prevented the development of a national medicine policy. The responsibility for medicine management falls under various state bodies with often overlapping roles and functions. A new legal framework is being set up with EC assistance, including a new medicine law (to be adopted by the end of 2002) and the establishment of a National Medicine Agency (NMA), which will be operational in early 2003.

Complementary and Past EC Assistance

Several related EU-funded projects are ongoing, including support to the pharmaceutical sector, development of clinical guidelines, assessment of health services, rehabilitation of medical equipment and reorganisation of blood transfusion services. The proposed 2003 programme activities will have close links with on-going EC funded projects. For example, the MoH will greatly benefit from two forthcoming EC funded studies aimed at assessing the status of health services and the national burden of disease on the health system. Both will provide invaluable inputs to the MoH staff for setting priorities and planning.

In addition, since 1999, the Commission has provided almost €30 million worth of EC humanitarian assistance for the health sector, including support to the primary health care system (with equipment, physical rehabilitation of primary health care facilities and training of health staff) as well as to the public health system (support to the communicable diseases' control system, and support to the Institute of Public Health). The proposed 2003 programme activities will be complementary to the assistance already provided.

Related Activities of Other Donors

Until recently, the lack of adequate leadership in the health sector has discouraged international donors from providing assistance. Close collaboration has been established with all relevant authorities and donors, in particular the Health Insurance Fund, Health Care Reform Commission, World Bank, DFID, WHO and, for the future, USAID, CIDA and EIB.

For more than one year, the Agency has worked in close collaboration with the World Bank and the HCRC in defining the guiding principles of the health care reform and the respective roles of each in supporting this process. More recently, the UNDP has joined this process. Short and long term interventions have now been agreed upon between the main stakeholders, including the preparation and implementation of a health master plan.

Project Activities (combined approx. €9.5 million)

6.1.4 .1 Ministry of Health Capacity Building Measures

Experts will enhance the capacity of MoH staff largely through assisting in (i) the reorganisation of the MoH; (ii) strengthening MoH's policy and planning function and (iii) designing and implementing a national plan for human resources' development.

They will also undertake feasibility studies related to hospital restructuring/rehabilitation and initially fund a Project Implementation Unit leading to an EIB health sector investment.

6.1.4.2 Public Health Capacity Building Measures

Experts will enhance the capacity of the Institute(s) for Public Health (IPH), Institute of Social medicine (ISM) and the MoH, essentially by assisting in restructuring the IPH system, preparing a national integrated public health strategy and action plan and supporting the professional development of key public health personnel.

6.1.4.3 Medicine Management Enhancement Measures

Experts will assist the MoH and Health Insurance fund (HIF) to (i) develop an integrated strategy for medicine management and an action plan for the development and implementation of a national medicine policy; (ii) assist in the development and implementation of new systems that will ensure more effective medicine management and cost-effective use of scarce resources and (iii) educate and train health workers.

The MoH will lead the process of policy and strategy formulation. Other health institutions, in particular the HIF and IPH, will be engaged in institutional capacity efforts and remodelling the systems of public health and medicine management.

6.2 ECONOMIC RECONSTRUCTION, REGENERATION AND REFORM (approx. €141.5 million)

The components outlined below deal with proposed programmes/projects in energy, transport, and environment as well as in the rural economy/agriculture, enterprise and local/ municipal development sectors.

6.2.1 Energy (approx. €69 million)

Background

At present, the electric power system in Serbia faces the consequences of more than a decade of lack of maintenance, under investment and damage due to the air strikes in 1999. The system is still operating at the edge of fundamental safety and reliability requirements with high levels of outage times for main equipment. Both the need to operate functioning plant non-stop and a lack of funds have inhibited overhauls and necessary maintenance, causing the system to deteriorate over a number of years. Many parts of the system are considerably overloaded. The existing generating capacity is unable to meet peak demand in the winter periods and the deficit has to be met by importing energy from surrounding countries in order to avoid power cuts. This problem has been exacerbated in 2001 and 2002 because the capacity of the hydro-plants was severely reduced earlier in the year due to unusually dry weather.

Further plant overhauls are necessary, so as to continue to assure that basic demand and reliability estimates are met. The proposed overhaul of Nikola Tesla A5, and the B1 steam reheat line, together with further support towards the successful completion of the current EC-funded power station project (TENT A3) will ensure

greater reliability and should contribute to a generation capacity of up to 1340 MW from the rehabilitated plant into the EPS system over a period of three years. The two major overhauls for Nikola Tesla Units A3 (under the 2002 Programme) and A5 will guarantee plant life extensions in excess of ten years.

The government has sought to improve EPS's finances to make it more self-sustaining by imposing substantial tariff increases. Even though new prices have increased by 233% from 0.9 US cents per kwh to 3.0 US cents per kwh over the last 18 months, they are still below the cost of production. Nevertheless, EPS's financial position should improve gradually as a result of the increases and provide additional resources for maintenance and overhaul programmes in the future.

It is generally accepted at government levels, and within EPS itself, that the current structure of EPS is unsatisfactory and that changes are necessary both in the organisation and the numbers of staff employed. There is a widespread need for training in modern management and specialist skills, especially in the areas of planning at all levels. In particular, system expansion and development strategies need to be developed using international best practice tools for new generation investments based on various fuels and technologies (coal, gas, combined cycle) as part of a Least Cost Investment Plan (LCIP), including integrated Combined Heat and Power schemes (CHP) among the options.

Integration issues of regional energy markets are pursued by the Agency, largely through the work undertaken by the South East Europe Regulatory Forum (SEERF) and the EC/Agency's assistance programme in establishing a Serbian Energy Regulatory Agency, which is one of the pre-conditions for the market to operate. The Agency is also actively participating in regional market energy conferences/workshops. Support for promotion of the Regional Electricity Market (REM)⁶ of Southeast Europe will be reflected in the implementation of the Agency's assistance in the sector.

Complementary and Past EC Assistance

Past EC assistance funded heating fuel and electricity imports during an emergency situation. Subsequently, it supported output in the generation, transmission and coalmines through the emergency rehabilitation programmes for 2001 and 2002. It then focussed on reducing electricity demand through the establishment of the Serbian Energy Efficiency Agency and guaranteeing longer term fuel supply (feasibility study of Tamnava West coal field). By helping to establish the Energy Regulatory Agency it also set in motion longer-term efficiency enhancements by enabling unbundling and privatisation of various activities.

Related Activities of Other Donors

All activities are undertaken in close cooperation with other donors, particularly the EBRD, EIB, World Bank and KfW, who form part of an ad hoc donor coordination group.

⁶ A Memorandum of Understanding on the regional Electricity Market in South East Europe and its integration in the European Internal Electricity Market was signed by the energy ministers from all countries in South-East Europe on 15 November 2002 in Athens.

Project Activities

6.2.1.1 EPS Capacity Building Measures (approx. €5.4 million)

Based on a thorough needs analysis, experts will (i) design and implement modern management and training programmes especially in the areas of planning at all levels; and (ii) develop a Least Cost Investment Plan (using modern optimisation techniques) as part of the institution-building project.

The duties and responsibilities of EPS, the Ministry of Mines and Energy and the Agency will be set out in a Memorandum of Understanding setting out the duties and responsibilities of the parties, such as contractual relationships, facilities to be provided by EPS and a commencement date. This is based on the model used in the Nikola Tesla A3 major overhaul under the 2002 EC funded energy programme.

6.2.1.2 Rehabilitation / Overhaul of Thermal Power Plants (approx. €63.6 million)

EC project funds will support the major overhaul of Nikola Tesla A5 (TENT A5), the B1 (TENT B1) steam reheat line, and the successful completion of the current EC-funded power station project (TENT A3). The duties and responsibilities of EPS, the Ministry of Mines and Energy and the Agency will be set out in a Memorandum of Understanding, such as the one used for the Nikola Tesla A3 (TENT A3) overhaul under the 2002 Energy Programme. The project will also fund the project's management engineer. Further details of the project are to be found in the accompanying project annex.

6.2.2 Transport (approx. €4.5 million)

Background

Serbia has an extensive transport infrastructure. However, the network has suffered from lack of maintenance over the past decade as well as from extensive war damage affecting road, rail and water transport systems. Moreover, unsustainable financial policies and inadequate use of existing funds have resulted in a significant de-capitalisation of Serbia's transport infrastructure. Institutional capacity has also been much weakened as systems and procedures for planning, monitoring, and managing transport activities were neglected or even misused. Institutions had to focus on coping with emergencies, leaving little room for developing and implementing long-term plans. Also, the Ministry of Transport and Communications of Serbia has not yet focused on harmonising related transport policies, laws and regulations with those of the EU and has not yet requested assistance in this matter. But EC/Agency staff are engaging the Ministry in reviewing current sector policies, laws and regulations in order to develop an action programme suitable for EC funding in 2004.

Considerable transport infrastructure investments (largely funded by the IFIs) are now underway or about to begin, some with the help of EC funded studies on the most important TEN corridors. Essentially, much of these investments focus on priority road re-surfacing and railway track upgrading. More ambitious investments, especially for large transport infrastructure projects, require thorough study taking into account

economical and financial analysis, environmental impact assessment and detailed technical specifications. Such studies take time and in turn the projects often need time to mature before investment decisions can be taken. As a consequence, the EC's 2003 transport sector programme proposes to fund three large feasibility studies, having high priority for the Serbian government and the IFIs as possible future investments.

Complementary and past EC assistance

The EC funded 85% of the cost (€25 million) of the Danube Commission's project to clear the Danube at Novi Sad of debris and un-exploded ordnance. The EC has subsequently funded the reconstruction of the Sloboda Bridge and a number of feasibility studies and technical assistance linked to on-going IFI investments in rail/road/airport rehabilitation and capacity building (€44 million). The French government has funded a Transport Infrastructure Regional Study (TIRS1). The EC is also financing regional studies in the transport sector, such as the ongoing Regional Balkans Infrastructure Study (REBIS), and possible environmental investments in the Danube river basin.

Related Activities of Other Donors

Both the EIB and EBRD have large road/rail rehabilitation programmes underway (approx. €467m), which focus on improving the transport infrastructure on the strategic Pan European corridors. Greece (approx. €100m under the Hellenic Plan) and FRY/Serbia itself are also planning to provide funds to rehabilitate a number of other sections linked to the Corridor X road network between Nis and Kumanovo (in the north of FYR Macedonia).

Project Activities

6.2.2.1 Feasibility studies for (i) Belgrade City Bypass, (ii) Belgrade to Montenegro road and (iii) an Inland Waterways' Master Plan (approx. €4.5 million)

Experts will be engaged to prepare a new feasibility study for the *Belgrade City Bypass*, which will include a revised traffic forecast, an economic and financial justification, an environmental impact assessment including mitigation measures and careful analysis of the proposed alignment. The study will consider the impact on not only the ring expressway itself but also on the main urban road system as a whole.

The feasibility study of the *Belgrade/Montenegro* road will analyse different scenarios based on information provided from engineering and traffic surveys. The study will include the project's economic and financial feasibility, cost estimates for proposed road and tunnel rehabilitation and eventual construction of new road sections, including bypasses around towns and villages with the aim of strengthening the two Republics' economic links and of enabling a faster, safer and better flow of traffic.

The *Inland Waterways Master Plan* study will assess and identify priorities for funding infrastructure related to the Danube, Sava and Tisa rivers - such as rehabilitation of ports and their needs for adaptation to suit modern inter-modal transport operations and a general adaptation of the waterways to international standards. Restoring the river network would benefit all neighbouring countries.

Implementation of the project requires full commitment of the Ministry of Transport and Communications of Serbia and participation of senior management of the Road Directorate and the Belgrade Highway Institute. The Government agency PLOVPUT is the competent authority for river transport. It is responsible for the development and maintenance of inland waterways and it will act on behalf of the Federal Ministry of Transport.

6.2.3 Environment (approx. €12.5 million)

Background

Several years of neglecting problems related to the environmental sector have brought about a generalised state of moderate to severe pollution in the country, including industrial contamination and domestic generated waste. The 1999 air strikes compounded the environmental problems. This situation applies to air, land and water.

Recent sector policy changes introduced by the Government culminated in June 2002 with the establishment of a specific Ministry for the Protection of Natural Resources and Environment. Public awareness is being raised and appropriate legislation introduced in line with international and EU standards. A new framework law for Environmental Protection was prepared with support of the international community. The EC's DG-Environment has been involved in the preparation of the final text of the draft law, to be ratified during 2002. The new Ministry, however, is confronted with a weak institutional and legal framework coupled with limited financial and human resources. Thus, strengthening of institutional capacity on both central and local level is one of the main priorities. Specific attention in this respect will be needed for the establishment of a national environmental agency and an environmental inspectorate.

In addition, a certain number of UNEP identified "hotspots", i.e. localised situations of abnormally high environmental degradation have raised concern in the national and international community and triggered specific remedial action plans. One of the more serious "hotspots" is the Pancevo canal, which discharges industrial effluents into the Danube. Most of the degradation resulted from the air campaign compounding damage from previous industrial environmental neglect. The resulting contamination of the Pancevo canal has reached quite serious levels and presents a threat to both human health and locally to the eco-system of the Danube.

Complementary and Past EC Assistance

The EC funded capacity building measures in 2002 were designed to contribute directly to realising a number of the environmental priorities, notably through equipping Republican and municipal authorities with the expertise necessary to respond to the challenges of the new Framework Law on Environmental Protection. This programme will also facilitate the effective participation of civil society in new environmental protection processes and structures.

Related Activities of Other Donors

The proposed 2003 programme is especially designed to maximise synergy with ongoing initiatives of inter alia the OSCE, World Bank, UNEP/UNOPS, the Regional

Environmental Centre and bilateral assistance from Finland. The 2003 environmental programme will build on and consolidate the activities initiated by the 2002 capacity building programme.

In the case of the Pancevo canal, the rehabilitation of the canal itself is effective and sustainable only if the industrial effluent waters are pre-treated to an acceptable level at the industrial plants generating these wastewaters. Under the co-ordination of UNEP, this problem is also being tackled with funds (\$1m) provided under the UNEP Trust Fund through bilateral contributions from the Netherlands, Denmark, Finland, and others. Rehabilitation of the water treatment plants is already well advanced. Formal guarantees from UNEP will be obtained as a precondition for the present project, to the effect that the rehabilitation of the water treatment plants will be finished on time.

Project Activities

6.2.3.1 Environmental Capacity Building (approx. €8 million)

The EC will provide technical assistance to (i) the Ministry for Protection of Natural Resources and Environment in order to build staff capacity for implementing the full range of the forthcoming legislation; (ii) further support for the establishment of the Serbian Environmental Agency, based on the recommendations of the 2002 EC/Agency support programme; (iii) support the preparation of the National Environmental Action Plan in close co-operation with the World Bank

EC funds will also support (i) the preparation of five Local Environmental Action Plans in selected municipalities as well as the implementation of selected priority projects; and (ii) the preparation of two projects for possible tendering in 2004 (a Belgrade waste water project and an emission control project for coal fired power plants).

6.2.3.2 Pancevo Canal Rehabilitation (approx. €4.5 million)

This EC project will fund the supervising engineers and works contract consisting of constructing a landfill or alternatives, dredging and stockpiling of the sediment from the canal into a landfill or alternatives as well as remedial works. Adequate environmental measures will be taken to meet the environmental norms and standards of the European Union,

For the *capacity building* project, all project partners are expected to actively participate in its implementation, providing an agreed level of logistical support. EAR will sign Memoranda of Understanding with the Ministry, participating municipalities and the Environmental Agency detailing the required input from the project partners.

For the *Pancevo Canal* project, the lead local counterpart will be the Ministry for Protection of Natural Resources and Environment, which will bear the responsibilities of the Contracting Authority in the project (except financial responsibilities). The other main stakeholder will be the Municipality of Pancevo. The Ministry of Construction will issue the necessary construction licence for the works. The factories concerned will be construed as contractors to UNEP for the implementation of the remedial works at the water treatment plants.

A particular role of Special Project Advisor to the Agency will be assigned to UNEP, on account of its participation in formulating the project and co-ordinating the hotspots' rehabilitation countrywide.

Given the complexity of the structure of the stakeholders, an adequate level of participation and co-ordination will be necessary through the creation of a steering committee.

<p>6.2.4 - 6.2.6 Economic Development programme components (approx. €55.5 million)</p>

Three economic development programme components are outlined below. These are:

- *Rural economy / agriculture (6.2.4);*
- *Privatisation and Enterprise Development (6.2.5);*
- *Local / Municipal Economic Development (6.2.6)*

<p>6.2.4 Rural Economy / Agriculture (approx. €7 million)</p>
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Background

During 2002, the Serbian Government supported by the EC undertook a comprehensive analysis of the food chain safety system (veterinary, phyto-sanitary and sanitary control) in Serbia. Analysis of existing structures confirmed that a key coordinating role would need to be played by the existing Republican inspectorates to link policy, production, trade and laboratory analysis. However, lack of co-ordination between the different inspectorates, both between sectors and between the Republic and Federal levels, has led to duplication of efforts and failure to fully implement the necessary control measures. The operations of each inspectorate also need to be modernised and strengthened. In addition, reform of the inspectorates is given particular urgency by the need to recover and expand export markets for agricultural products. More comprehensive controls will give international trading partners confidence and satisfy the expectations of domestic consumers regarding food safety. A reform of the inspectorates in the near future is thus essential.

In this context, the existing Border Inspection Posts (BIPs) network also needs to be upgraded to ensure effective veterinary and phyto-sanitary control of imported food products, in line with EU procedures which require veterinary, phytosanitary and sanitary control to be completed at the border.

Improvements in the food safety chain system will be closely coordinated with Montenegro through intense cooperation between both Republics and at the Federal/Union level.

A vital part of the food safety chain system is also movement control of *animals and animal products*. An animal identification system would improve animal health surveillance and therefore enhance livestock production. Together with movement control, it would support disease, drug and residue monitoring programmes by allowing the tracing of animals back to their origin. Such an identification system

would also enable swift veterinary response to disease outbreaks and their control by facilitating identification of other potentially infected animals due to contacts in the livestock movement chain. Furthermore, it would strengthen the capacity of Serbia to trade with the EU and EU associated countries in animals and animal products, and reflects a similar approach to the corresponding programme in Montenegro. In the implementation phase, the respective programmes will be jointly coordinated to ensure compatible strategies, policies and systems are applied within both entities and follow state level policies in this field.

Complementary and Past EC Assistance

The proposed projects are a logical continuation of previously EC funded projects in agriculture, including the review and restructuring of the related laboratory network and the funding of laboratory equipment (2002-3). This on-going project will closely link and complement the proposed EC projects on reforming food chain laboratories and on animal identification planned to commence in 2003.

An animal identification system is currently being introduced in parallel with EC/Agency actions in Kosovo and FYR Macedonia. Montenegro will begin to address the issue as well.

Related Activities of other Donors

The proposed project will work closely with the ongoing US Department of Agriculture programme of training courses and seminars, the USAID and EC funded WTO assistance programmes (non-tariff barriers), as well as with the Netherlands assistance in the veterinary sector (review of artificial insemination).

Project Activities

6.2.4.1 Capacity Building for the Agricultural Inspectorates (approx. €5 million)

Expert assistance will be provided to: (i) review the structure, functions, management, staffing and resources of the sanitary, phyto-sanitary and veterinary inspectorates; (ii) develop a model for a reorganised, restructured system of inspectorates with well-defined functions and without overlaps; (iii) assess current legislation relating to the work of the inspectorates and draft new legislation/regulations/amendments appropriate to the functioning of the reformed services; (iii) develop an inspectorate staff-training programme to train the inspectorate to international standards; (iv) co-ordinate and supervise the delivery and installation of equipment and infrastructure procured by the project for ten selected Border Inspection Posts (BIPs), and (v) ensure an overall effective and efficient operation.

Project partners will be the Ministry of Agriculture and Water Management and the Ministry of Health. The appointed experts will work in close co-operation with the project partners at all stages of implementation.

6.2.4.2 Introduction of an Animal Identification System (approx. €2 million)

The project will provide expertise to essentially: (i) develop an overall strategy for the introduction of an animal identification and movements' system, taking into account

the characteristics of Serbian livestock production and the opportunities/constraints presented; (ii) develop an implementation plan for the introduction of the system to include technical, financial and human resource requirements; (iii) review current legislation required for the introduction of the system and prepare draft legislation/regulations/amendments necessary for effective implementation and harmonisation of these provisions with EU legal requirements; (iv) assist in the development of operational procedures for implementing the scheme; (v) assist in the selection, procurement and installation of suitable computer hardware and software required to implement the system; and (vi) assist with the recruitment and training of staff .

The project partner will be the Ministry of Agriculture and Water Management. The overall project will be implemented in close co-operation with the Ministry and in particular the Veterinary Department. The Ministry will approve the overall strategy and implementation plan and the Veterinary Department will take the lead role in the scheme's phased implementation. The Government will provide for adequate funding to run the system and will develop and adopt appropriate legislation.

6.2.5 Privatisation and Enterprise Development (approx. €13.5 million)

Serbia's enterprise sector comprises a significant number of large Socially-Owned Enterprises (SOEs) and an active private sector of some 60,000 SMEs. The SOEs have continued to make losses during the '90s and generate a substantial quasi-fiscal deficit, which burdens the economy and the financial sector. Their disposal, primarily through *privatisation*, is a keystone of the Government's programme of structural adjustment and economic reform, and a prime determinant of their success.

In 2002/3 the Privatisation Agency (PA) plans to privatise some 850 enterprises, complete the privatisation of another 500 by tender or auction, implement an auction of thousands more, and restructure 49 of the large SOEs, from which it is hoped that a number of viable enterprises will evolve. Without additional assistance the PA will not be able to realise these ambitious plans.

Several related issues will emerge during this process. The depressed nature of the *enterprise sector* will significantly inhibit the privatisation process. Necessary restructuring of overstuffed and inefficient companies will lead to further large-scale unemployment and the need for welfare and retraining provisions for the labour force. Experience suggests that a *focus on SMEs* (approx. 50 – 250 employees) and restructuring the largest companies into potentially viable SMEs is the most effective way of developing net contributors to the economy.

As the economic transformation continues, interest in *regional economic development policies* has increased especially as an instrument for tackling the transformation's negative side effects. Development of new labour market orientation and skills' development mechanisms are required in order to increase the level of entrepreneurship, employability and adaptability of the labour force, particularly of disadvantaged groups. There is an urgent need to define pilot interventions in the field of regional economic development policy in order to improve local economic and social development and to promote institutional capacity building, especially in areas with a high concentration of refugees and IDPs.

Exporters face formidable obstacles within Serbia. Typical problems include: lack of capital and technology; lack of understanding of marketing and international markets;

low levels of product development and lack of certification; expensive working capital and high cost of pre-export finance, etc. Government needs to address such export barriers and assist companies to exploit opportunities.

In February 2001, the Government established the Serbian Investment and Export Promotion Agency (SIEPA) with an initial operational emphasis on attracting investment. Government now plans to strengthen the export development division of this Agency.

Complementary and Past EC Assistance

The proposed activities are fully consistent with, and complementary to other ongoing enterprise related EU funded projects such as in the areas of SME policy and strategy, privatisation, business support services, SME credit facilities, training and re-training for unemployed and redundant employees. All the proposed activities take account of ongoing EU support to the Ministry of Economy and Privatisation on SME policy and a national SME development strategy. Outcomes from the proposed *Regional Economic Development* Programme will be closely coordinated with the proposed Local/Municipal Development Programme.

Related Activities of Other Donors

Other donor related activities include: privatisation, institutional development and enterprise sale related initiatives (World Bank, USAID, DFID, KfW and GTZ), provision of business advisory services (GTZ, Swiss Development Corporation, SEED); the EIB Global Loan Facility; EBRD, Italian Government and German and Russian bank funded credit lines. Close coordination will also be made with the upcoming World Bank funded projects in investment promotion and labour policies, USAID funded projects in local government reform and related SIDA activities.

Project Activities

6.2.5.1 Further Support to the Privatisation Agency (approx. €5million)

The EC will assist in establishing decentralised privatisation agencies including support for initial operating costs, staff training and an "Expert Fund" which will finance an in-house team of privatisation advisers and short-term expertise to assist in completing and finalising related post-sale formalities (mostly legal and financial). Support will also be provided to the Republican Development Bureau for advanced training in short- and medium-term economic forecasting.

6.2.5.2 Pre- & Post-Privatisation Restructuring (approx. €2 million)

EC funds will support the 'Turn-Around Management' (TAM) Group based at EBRD to assist about 25 enterprises. Depending upon the pipeline and screening of the proposed enterprises, the proportion of eligible pre- and post-privatisation candidates will be determined in conjunction with the Ministry of Economy and Privatisation and the Chambers of Commerce.

6.2.5.3 Regional Economic Development (approx. €4 million)

EC funds will facilitate in targeted regions the capacity of local institutions to undertake economic development activities such as: integrated regional development

strategies, which may target actions related to improving employability, market access and social development. Areas with high percentages of vulnerable population (eg internally displaced persons and refugees) will be among those to be prioritised in the targeting considerations.

EC funds will also be used to co-finance activities of a *Regional Socio-Economic Development Fund*. Co-financing assistance will be provided to these selected regions for projects of socio-economic and regional importance.

6.2.5.4 Export Development Programme (approx. €2.5 million)

EC funds will support capacity building activities of SIEPA and selected enterprises in export development, such as: staff development; short and medium-term export strategies and action plans reflecting best EU practices, promotion of SIEPA to client companies, and business organisations, development of an export development advisory service and a trade information service as well as cost-share a *Marketing Development and International Linkages Programme* for enterprises.

The Privatisation Agency will be responsible for implementing the proposed *privatisation activities* as outlined in a Memorandum of Understanding. For the *SME development project*, the main project partners are the Ministry of Economy and Privatisation, the Privatisation Agency and the Chambers of Commerce, which will assist with enterprise screening and selection on the basis of potential viability. *SIEPA* will be the main project partner and ensure its sustainability. For the *Regional Economic Development* project, the main project partners are the local authorities, labour market bureaus and the Ministry of Labour and Education.

Each project will also have a Steering Committee ensuring participation of various project partners, programme linkages and follow-up on successful reform actions.

6.2.6 Local / Municipal Economic Development (approx. €35 million)

Background

Many years of centralised policies/decisions, isolation and economic decline have brought municipalities into an extremely difficult situation. Municipal annual revenues are low, currently varying between €10 - 40 per capita. Municipalities have difficulty in developing the concept of local government as "a service to citizens", due to a lack of both legal authority and resources required for adequate service provision. In summary, local government is facing a poor and still centralised administrative framework, a difficult economic environment, poor public services and a lack of efficient municipal management. In some municipalities, these difficulties are further aggravated by the pressure from large IDP and refugee populations,

As a response, Serbia is now in the process of launching an administrative reform programme, including both the decentralisation of responsibilities and financial resources to the municipal level and the development of regional policy. A new law on Local Government has been adopted by the Parliament in February 2002, and a new Ministry of State Administration and Local Self-Government (MSA/LSG) was recently established.

Currently, the delineation between central and local/municipal government is unclear and incoherent. Moreover, the fiscal system does not provide adequate or dependable sources of municipal revenues. Mechanisms for citizen and civil-society participation in

local governance are inadequate. As the new Law on Local Government has been only recently adopted this situation is likely to change. But in order for the law to be effective it will need to be supplemented with laws on primary education, social care and municipal property.

Complementary and Past EC Assistance

The EC has initially supported municipalities in Serbia through the 'Schools for Democracy' and the subsequent 'Towns & Schools for Democracy' programmes, both forerunners of the proposed 2003 Local/Municipal Development and the Regional Economic Development programmes. Close coordination will be made with two other complementary programmes currently funded by the EC and implemented in the same region (the SME Advisory Boards and Civil Society projects).

Related Activities of Other Donors

Various other important programmes in municipal support are underway or planned by other donors (notably USAID, EBRD, KfW, UNDP, SIDA, SDC and others). The programme is designed to complement and increase synergy with ongoing municipal support programmes (the project will work directly with the EBRD and KfW on the aspect of loan finance for municipal infrastructure and will consolidate on the activities of the UNDP implemented REP and SSMIRP programmes).

Project Activities

6.2.6.1 Support to Municipalities and Administrative Decentralisation (approx. €35 million)

EC funds will assist the Government's decentralisation process by supporting a Local/Municipal Development Programme consisting of four related projects:

- *A Municipal Support Programme (MSP)*, which will promote effective decentralisation and participation, stimulate local economic development, contribute to the improvement of public services and improve municipal management;
- *Support for a Municipal Infrastructure Agency (MIA)*, which will be established by the Ministry of Finance in order to enable municipalities and local public utility companies to access financial resources for creditworthy infrastructure projects. The project will also provide complementary grant finance for selected infrastructure projects linked to IFI investments;
- Support for the *City of Belgrade* to assist in the development of a *Public Private Partnership (PPP)* project for water and waste water treatment in Belgrade; and
- Support for a *Municipal Improvement and Revival (MIR)* project, which aims to provide further support for confidence building measures in line with the Government's efforts to achieve durable political stability and social and economic recovery of southern Serbia.

Serbia's more disadvantaged areas, as determined by refugee/IDP socio-economic assessment studies, are included in the targeting for this municipal development programme.

All project partners are expected to actively participate in the implementation of the programme and provide an agreed level of logistical support. The agency will sign a Memorandum of Understanding defining responsibilities with the Ministries (MPALSG & Ministry of Finance), the participating municipalities (including City of Belgrade) and the EBRD.

6.3 SOCIAL DEVELOPMENT AND CIVIL SOCIETY (approx. €24 million)

The sections below describe proposed projects for Vocational Education and Training (VET), Civil Society, Media and the EC managed Tempus higher education programme.

6.3.1 Vocational Education and Training - VET (approx. €13 million)

Background

The Government of Serbia is engaged in an economic restructuring process with implications for the labour market, requiring a competitive and flexible workforce able to change jobs over the course of the working life or to become self-employed in new emerging sectors of the economy. Vocational education and training (VET) will therefore have a dual role to play during this process: (i) to provide different sectors of the economy with a well-skilled labour force required to improve competitiveness, and (ii) to provide unemployed and redundant people with new skills and competencies to facilitate their employability.

VET reform is still at an early stage of development. In 2001 the Ministry for Education and Sports (MoES) delivered a draft strategic framework for reform. Its broad aims include creating new and more flexible links between VET and the labour market, boosting and diversifying funding, updating curricula in line with the changing demands of the economy, achieving a better balance between general and vocational education, improving vertical and horizontal mobility within and out of VET and reorganising teacher training. Plans are afoot to create two institutions to oversee the reform process – a National VET Council and a Centre of VET focussing on VET system development, quality improvement and human resource management in the sector. Adult education will be strengthened by establishing a network of institutions (through transforming five selected VET schools into regional training centres for adults) to respond to the needs of initial VET for adults, job-related training for employed people, reconversion training for unemployed, and enhanced employability for all through an emphasis on general knowledge and new basic ("soft") skills.

The European Training Foundation has played a major role in identifying and preparing the proposed VET programme.

Complementary and Past EC Assistance

Synergy will be established with the on-going 2002 EC project for support to human resources' development measures for the unemployed and the newly redundant, which will cover the implementation of active employment measures, including training, in the Sumadija region. Initial results of this programme will also be fed into the design of the proposed 2003 Regional Economic Development Programme.

Related Activities of Other Donors

Links will also be established with the World Bank project “Labour Learning and Innovation Loan” starting in 2003 and with forthcoming EIB investments in the education sector. Other active donors are Finland (teacher training) and GTZ (VET - business administration).

Project Activities

6.3.1.1 Vocational Education and Training

This EC project will facilitate *policy and strategy* development through capacity building of local actors, development of VET legislation, financing and governance, streamlining of the VET school network, and adult training. Support will also be provided to establish and operate an *innovation fund* aimed at promoting participation in the process of modernisation at grassroots level. It complements a WB project having a similar component. Support will also be provided for the *rehabilitation of school buildings* for selected schools as well as *equipment* for demonstration schools for upgrading of workshops and laboratories, didactical equipment, etc. The project will also assist EIB in preparing, tendering and monitoring education sector related investment preparation activities.

The MoES will be the main beneficiary of the programme and will ensure its sustainability through the adoption of adequate measures. A high level Steering Committee and working groups at central and local levels will be established ensuring the participation of various project partners in designing and following up on all the VET and adult reform actions.

6.3.2 Civil Society (approx. €1 million)

Background

Over a quarter of the state's (excluding Kosovo) eight million people live in poverty while an additional 20% are near poor. As a result of conflicts, 600,000 refugees and internally displaced persons (IDPs) live in FRY, representing an additional “burden” and concern in the current difficult economic circumstances. Other most affected groups, according to the assessments of the Serbian Ministry of Social Affairs, are the pensioners (1.5 million), and the unemployed (750,000). The EC/Agency acknowledges the potential gap between the end of humanitarian assistance and economic recovery and has endeavoured to take this into consideration.

In April 2002, Serbia prepared a draft Poverty Reduction Strategy Paper (PRSP). The central objective of a country's PRSP is to try to ensure that policy actions to increase growth and reduce poverty are integrated into a coherent macro-economic framework after extensive consultations with national stakeholders. Serbia and Montenegro completed *Interim* PRSPs by June 2002. The Ministry of Social Affairs is the lead ministry in the PRSP process in Serbia. Design of the final PRSP documents began in September 2002 and the strategy should be completed by the end of July 2003. The implementation of the PRSP is planned to start in August 2003. The Serbian government recognised the PRSP as an opportunity to create a national economic development strategy, which helps vulnerable groups. One of the key concerns, given the financial constraints on the budget, is how to balance support for economic

growth and employment with the provision of social assistance to the poor and vulnerable populations during the period of transition.

The Serbian government and non-government organisations have recently agreed that a consultative and participatory process is essential for the development of a comprehensive PRSP strategy. As participation of civil society organisations in the PRSP process is one of the key requirements of the World Bank and IMF, the Serbian Government requested assistance to facilitate inclusion of civil society organisations in the design, implementation and monitoring of the PRSP.

Complementary and Past EC Assistance

The EC has supported a number of projects that are directly or indirectly related to the poverty alleviation process: for example, programmes dealing with economic growth (enterprise development), reforms of labour and social policy, public health, the improvement of basic services at the local level through various municipality programmes and support to NGOs' activities dealing with social and economic issues. This programme will also build on the provision of previous basic humanitarian assistance, implemented by ECHO, that was targeted at the poorest strata of society.

Related Assistance of Other Donors

From April 2002, the World Bank engaged Serbia and Montenegro in the PRSP process through a Poverty Trust Fund for Serbia and Montenegro. DFID also support the process by allocating funds to the PSRP Management Unit. UNDP will facilitate consultations between the civil society organisations and the Government, while the Norwegian Government will contribute to a Social Innovation Fund to Fight Poverty.

Project Activities

6.3.2.1 Inclusion in Poverty Reduction Strategy Process (approx. €1 million)

The project will facilitate a process of consultations between the government and civil society organisations in a staged process of elaborating the overall poverty reduction strategy paper (PRSP) and the establishment of the Management Unit of the Social Innovation Fund to Fight Poverty (SIFFP) with the Ministry of Social Affairs.

As a commitment to the PRSP process, the Government will allocate minimum €1.6 million from the 2003 budget. Further Government allocations are expected to come from the Lottery revenues and will increase each year. UNDP will take a lead coordination role in institutionalising the policy dialogue process between the government and civil society organisations and support implementation of PRSP through establishment of a Management Unit for the SIFFP.

6.3.3 Media (approx. €6 million)

Background

In Serbia there are 641 print media, 253 TV stations and 504 radio stations serving some eight million people. They operate in a small and unregulated market with low purchasing power. Most are still financed by the central government, municipalities or in some instances by donors. It is difficult if not impossible for most media to survive

solely on commercial revenues. In essence, the media landscape remains unchanged largely due to the absence of a coherent media policy and the delay in adopting a set of media laws. So far only the Broadcasting Act has been adopted. Other important laws, such as the Telecommunication Act, the Public Information Act and the Access to Information Act have not yet reached the Parliamentary agenda.

Complementary and Past EC Assistance

For many years, the EC has played an important role in actively supporting the country's independent media. It provided emergency support during the critical period enabling independent media outlets to continue their operations. After October 2000, the EC continued to be active in the media sector by providing support for the establishment of a new legal framework, participating in the restructuring of the state-run media and facilitating the independent media to continue their professional work during the current transition period.

Related Activities of Other Donors

Over the past few years, a large number of donors have been actively involved by providing crucial financial support for the survival of independent media, such as the Open Society Institute through its Regional Media Programme and the local Fund for an Open Society, the Swedish Helsinki Committee, the USAID/OTI and IREX ProMedia, the Swiss MedienHilfe, the Norwegian People's Aid, the Dutch Press Now, UNESCO. The Council of Europe and OSCE were active in developing the new legal framework for the media in Serbia and contributed to the drafting of important media laws, such as the Broadcasting Act, the Public Information Act and Access to Information Act.

Project Activities

6.3.3.1 Support to the Media Sector (approx. €6 million)

EC funds will be used to further the *transformation of RTS* into an independent and financially sustainable broadcasting service by targeting several investments facilitating the restructuring process.

Further EC funds will be used to support the *independent media* with the aim of strengthening those media outlets that have the potential and have shown willingness to adapt to the new market conditions, in particular for the Media Centre (a media service provider) and B92 (a major independent electronic media). In both cases, EC funding will assist their respective business plans (2002 to 2005) by providing training, technical assistance to improve management capacity and programming, IT related equipment, and the establishment of a "Media Fund" which will provide grants to local media to stimulate development of high quality programmes.

The project partners B92 and Media Centre will be responsible for the implementation of all activities as outlined in detailed project proposals to be annexed to Grant Agreements. The project partner RTS will chair the project steering committee and take a leading role in the implementation of the proposed restructuring process of the company, supported by consultants, the OSCE and the EAR. The OSCE will provide a co-ordinating role for donor support to the RTS and will liaise with the Agency regarding specific programme implementation issues.

6.3.4 University Education: Tempus (approx. €4 million) - Commission managed

Background

Within the framework of the general economic reform objectives of the European Commission's programmes for support to the non-associated countries and the Partner States of Eastern Europe, Central Asia and Mongolia, Tempus III aims to promote the development of the higher education systems in the partner countries through balanced co-operation between higher education institutions in the partner countries and the Member States of the European Union.

A priority for higher education systems in all South-East Europe is the achievement of the objectives of the so called Bologna Declaration, which was originally signed by 29 European governments and which aims at the establishment of a common European higher education space by 2010. Its objectives include the establishment of a common degree system in Europe (Bachelor, Master, Ph.D.), the introduction of the European Credit Transfer System (ECTS), the strengthening of a European dimension in quality assurance and the removal of obstacles for the mobility of students and staff.

Project Activities

6.3.4.1 EC Support for the Tempus Programme (€4 million)

The programme aims at funding Joint European Projects (JEPs) and Individual Mobility Grants. Joint European Projects can focus on: University Management; Curriculum Development; Institution Building and Multiplier Projects and can be implemented on a regional level, e.g. projects which include higher education institutions not only from one but from several of the eligible Tempus partner countries.

Tempus III: The European Commission's Directorate-General for Education and Culture has the overall responsibility for the policy and management of the Tempus Programme. Following an annual call for proposals, projects are assessed academically and technically according to general criteria and a list of national priorities established in co-operation with the partner country authorities, and taking into account the objectives of the Stabilisation and Association Process and the policy objectives of EU co-operation with the Tempus partner country. In implementing the programme, the Commission is assisted by the Tempus Committee, set up by the Council Decision on Tempus III and consisting of representatives of the Member States.

6.4 OTHER

6.4.1 General Technical Assistance Facility (GTAF); and Programme Reserve (combined total of approx. €5 million)

The main purpose of the General Technical Assistance Facility (GTAF) 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, tender evaluations; (ii) audits, monitoring, thematic / programme/project evaluations; and (iii) project preparatory and start-up actions.

The Programme Reserve component will be used to cover currently unforeseeable programme related expenditures. In addition, it could also be used in support of the "2003 Strategy for Sustainable Returns presented by the United Nations Mission in Kosovo in the Donor Co-ordination Meeting hold in Brussels on 5 November 2002. These projects would be complementary to the funds allocated in the Kosovo programme in order to ensure a trans-boundary dimension to the Agency's intervention in this area.

7. PROGRAMME IMPLEMENTATION

The Action Programme will be implemented as follows:

Implementation & Management

1. The Financing Agreement shall be concluded by 31 December of the year following that of the budgetary commitment.
2. The end of the implementation period of the Financing Agreement is hereby set at **31.12.2007**.
3. Any balance of funds remaining available under the EC Grant shall be automatically cancelled 18 months after the end of the implementation period of the Financing Agreement.

Contracts financed under this programme shall enter into force no earlier than the signature of the Financing Agreement in due form by the competent signatories, and no later than 3 years starting from the date of the budgetary commitment. Therefore:

- Any relevant contract or grant must have entered into force, having been signed by all the relevant parties, by this expiry date.
- Any contracts or grants that have not been entered into force, having been signed by the signature of all the relevant parties by this expiry date will not be finalised but will be cancelled and considered null and void.
- Any balance of funds under this programme that has not been used to fund contracts or grants that are in force by this expiry date will be de-committed as soon as possible thereafter.
- No addenda adding funds from this programme to any contract or grant may be entered into after this expiry date.

This annual programme will be implemented under the responsibility of the European Agency for Reconstruction (except for the Customs & Taxation, and Tempus III projects).

Implementation of projects will be carried out in close co-ordination and consultation with the beneficiary authorities and those international agencies and donors that are active in the various fields covered by the EC programme.

Tempus III: The European Commission's Directorate-General for Education and Culture has overall responsibility for the policy and management of the Tempus Programme. Following an annual call for proposals, projects are assessed academically and technically according to general criteria and a list of national priorities established in co-operation with the partner country authorities, and taking into account the objectives of the Stabilisation and Association Process and the policy objectives of EU co-operation with the Tempus partner country. In implementing the programme, the Commission is assisted by the Tempus Committee, set up by the Council Decision on Tempus III and consisting of representatives of the Member States.

A Financing Agreement corresponding to this Financing Proposal will be concluded with the counterpart authorities.

Tendering and Contracting

The contracts for services, works and supplies shall be concluded in accordance with the tendering and contract award procedures laid down in the Financial Regulation and other relevant instructions.

Monitoring, Evaluation and Audit

This programme (except for the Customs & Taxation and Tempus III programmes, which the Commission will implement) will be supervised and monitored by the Agency which will:

- (i) supervise the implementation of the programme components on the basis of regular reports, contacts with stakeholders and site visits;
- (ii) carry out regular monitoring and evaluation to follow the progress of the programme and its components, as well as ex-post evaluation after the completion of the programme.

The accounts and operations of the programme components may be checked at intervals by an outside auditor contracted by the Commission without prejudice to the responsibilities of the European Antifraud Office (OLAF) and the European Union's Court of Auditors.

8. GOVERNMENT COMMITMENT / CONDITIONALITIES

Assistance is provided on the basis of the existence of the necessary elements for the continuation of co-operation assistance, in particular, the respect of the SAP political and economic conditionality.

In addition to the SAP related conditionality, programme/sectoral/project conditionality may be imposed. Any programme, sectoral and/or project conditionality will be defined in the Financing Agreement / Memorandum to be signed between the Commission and the beneficiary authorities. Failure to comply with any defined conditionality may lead to delay, suspension or cancellation of the planned or committed assistance.

9. INDICATIVE DISBURSEMENT SCHEDULE (€ millions, accumulated)
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Sector	June 2003	Dec 2003	June 2004	Dec 2004	June 2005	Dec 2005	June 2006	Dec 2006	June 2007	Dec 2007
Public Administration Reform, incl JHA	1.7	4.4	7.3	10.9	17.5	32.5	34.8	40.7	41	44
Public Admin – Health	0.4	0.9	1.6	2.5	4	7.1	7.6	9	9.1	9.5
Customs & Taxation (Commission managed)	0.2	0.5	0.9	1.2	2	3.8	4.2	4.8	4.9	5
Energy	2.6	6.7	11.5	16.9	26.6	49.8	56.1	65	67	69
Transport	0.2	0.4	0.8	1.1	2	3.5	3.6	4.3	4.4	4.5
Environment	0.5	1.3	2.1	3.1	5	9.7	10.2	11.9	12	12.5
Rural Economy/Agriculture	0.3	0.7	1.2	1.8	3	5.3	5.9	6.7	6.9	7
Privatisation and Enterprise Devt	0.5	1.4	2.3	3.4	5	10.5	10.8	13.1	13.3	13.5
Local/Municipal Development	1.4	3.6	6.1	8.8	14.5	26.7	29.1	33.3	34	35
Vocational Education and Training	0.5	1.3	2.2	3.3	5	9.8	10.4	12.4	12.7	13
Civil Society and Media	0.3	0.7	1.2	1.7	3	5.4	5.6	6.6	6.8	7
General Technical and Administrative Facility ; Reserve	0.16	0.3	0.5	0.8	1.2	2.4	2.4	2.8	4	5
TOTAL	8.8	22.2	37.7	55.5	88.8	166.5	180.7	210.6	216.1	225

Tempus (Commission managed)	Dec 2004	Dec 2005	Dec 2006	Dec 2007
	1	3	3.8	4

Grand Total: 225 + 4 = €229 million