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CROATIA 2009 PROGRESS REPORT

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TO THE EUROPEAN PARLIAMENT AND THE COUNCIL**

Enlargement Strategy and Main Challenges 2009-2010

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COMMISSION STAFF WORKING DOCUMENT

Croatia 2009 Progress Report

1. INTRODUCTION

1.1. Preface

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

This report on progress made by Croatia in preparing for EU membership largely follows the same structure as in previous years. The report:

- briefly describes the relations between Croatia and the Union;
- analyses the situation in Croatia in terms of the political criteria for membership;
- analyses the situation in Croatia on the basis of the economic criteria for membership;
- reviews Croatia's capacity to assume the obligations of membership, that is, the *acquis* expressed in the Treaties, the secondary legislation, and the policies of the Union.

The period covered by this report is from early October 2008 to mid- September 2009. Progress is measured on the basis of decisions taken, legislation adopted and measures implemented. As a rule, legislation or measures which are under preparation or awaiting parliamentary approval have not been taken into account. This approach ensures equal treatment across all reports and permits an objective assessment.

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

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

1.2. Context

The European Council of June 2004 granted the status of candidate country to Croatia. Accession negotiations with Croatia were opened in October 2005. The Stabilisation and Association Agreement between Croatia and the EU was signed in October 2001 and entered into force in February 2005.

¹ The rapporteur for Croatia is Mr Hannes Swoboda.

² Enlargement Strategy and Main Challenges 2009-2010 (COM(2009) 533 of 14.10.2009).

1.3. Relations between the EU and Croatia

Croatia is participating in the Stabilisation and Association Process.

Accession negotiations with Croatia have continued. Negotiations have been opened on 28 out of 35 chapters (*science and research; education and culture; economic and monetary policy; enterprise and industrial policy; customs union; intellectual property rights; right of establishment and freedom to provide services; company law; statistics; financial services; financial control; information society and media; consumer and health protection; external relations; financial and budgetary provisions; TENs; transport; energy; free movement of workers; social policy and employment; free movement of goods; public procurement; justice, freedom and security; taxation; free movement of capital; regional policy; food safety, veterinary and phytosanitary policy; agriculture and rural development*) and provisionally closed on twelve (*science and research; education and culture; enterprise and industrial policy; external relations; EMU; IPR; information society; TENs; customs union; company law; statistics; free movement of workers*).

In addition, there are currently six draft EU negotiating positions in Council. Of these three are opening positions (*environment; foreign, security and defence policy; fisheries*) and three are closing positions (*consumer and health protection, financial services, energy*).

In its communication on enlargement strategy adopted on 5 November 2008, the Commission proposed an indicative road map for reaching the final stage of accession negotiations with Croatia. The Commission stated that it should be possible to reach this final stage by the end of 2009, provided Croatia fulfils all the necessary conditions. Croatia has made good overall progress in line with the roadmap. The roadmap has successfully galvanised efforts in Croatia aimed at meeting the benchmarks in order to open and close the chapters according to the indicative timetable of the roadmap.

However, the border issue between Slovenia and Croatia held back the accession negotiations such that a substantial number of chapters could not be opened or closed until October 2009, although technically finalised earlier. The Commission has provided its facilitation services to settle this dispute, which should remain a bilateral issue. Intensive efforts by the Commission, supported by the Trio of Presidencies, have been made over six months, which paved the way for a political agreement between the two parties reached in September 2009. The Commission welcomes the recent progress that led to a substantial number of chapters being opened and closed at the Inter-governmental conference in October. Bilateral issues should not hold back the accession negotiations.

Moreover, delays in Croatia itself in certain areas mean certain chapters have not progressed in line with the roadmap. This concerns in particular the opening of chapters on *the judiciary and fundamental rights* and *competition*, but also the closing of chapters such as *transport*.

Notwithstanding this, overall the progress achieved in Croatia in numerous chapters means that technical preparations in the negotiations are now nearing their final phase.

The **political and economic dialogue** between the EU and Croatia has continued. Political dialogue meetings were held in Luxembourg in April at ministerial level and in Brussels in June 2009 at senior official level. Economic dialogue meetings were held in Luxembourg in April at ministerial level and in July 2009 at senior official level. These meetings focused on the main challenges faced by Croatia under the Copenhagen political and economic criteria and reviewed progress being made towards fulfilment of Accession Partnership priorities.

Implementation of the **Stabilisation and Association Agreement (SAA)** has been uneven. Positive developments in the shipbuilding and taxation area have been recently accompanied by measures creating difficulties for EU operators when exporting to Croatia. With regard to State aid provisions, in particular as regards aid granted to the shipbuilding sector, the issue has now been largely resolved with the publication of tenders for the shipyards in difficulty with a view to their restructuring through privatisation. Croatia has also eliminated the discriminatory taxation of cigarettes (see Chapter 16). Following the entry into force of amended legislation in February 2009, EU nationals are now entitled to acquire ownership rights over real estate under the same conditions as Croatian nationals, in line with the obligations under the SAA. Following turbulence in the global financial markets, Croatia has applied the safeguard clause of Article 60(4) to postpone the liberalisation of certain short-term capital movements. In recent months, a number of measures applied by Croatia have resulted in increased import duties on a number of products exported from the EU. Discussions are ongoing to address these issues in the framework of the SAA.

The EU provides guidance to the authorities on reform priorities through the **Accession Partnership**. Progress on these reform priorities is encouraged and monitored through the bodies of the SAA. The SAA Association Council met in April 2009 and the SAA Association Committee in December 2008. Seven sectoral sub-committee meetings have been held since November 2008. Based on the Accession Partnership, Croatia adopted its national programme for EU accession in spring 2009.

Financial assistance is provided under the new Instrument for Pre-accession Assistance (IPA) from 2007. The 2009 IPA programmes amounted to € 151 million. This assistance is concentrated on institution building and preparation for the implementation of the EU's common agricultural policy and cohesion policy. In addition, Croatia continued to benefit from regional and horizontal programmes. Croatia has taken a number of important steps to address weaknesses identified by the Commission in Croatia's management of pre-accession aid. These steps have led to conferral on Croatia of decentralised management powers for IPA components I to IV. A track record of improved implementation is needed.

EU financial support has been provided to **civil society** development under the Civil Society Facility. A € 2.5 million grant scheme was set up under IPA 2009 with the aim of providing civil society organisations with the knowledge and skills to enhance their role in the fields of democratisation, human rights and refugee return, as well as promoting innovative social service delivery programmes. In addition, a € 16 million contribution under the Cross Border Cooperation programmes with Italy, Slovenia, Hungary, Serbia, Montenegro, and Bosnia and Herzegovina as well as participation in ERDF programmes will promote dialogue with local and regional authorities. Croatia's participation in an increasing number of Community programmes (11) is also an important tool to implement civil society dialogue.

In response to the economic crisis, an IPA **crisis package** has been created, comprising €200 million for the Western Balkan region which are expected to leverage investments of at least €1 billion, co-financed by the partner financial institutions. The country will benefit from a share of multi-beneficiary funds for competitiveness, SMEs, energy efficiency and banking sector regulation. As a candidate country, Croatia has been benefiting since 2007 from funding under IPA component III (roughly € 142 million cumulated since that year) for reinforcing the competitiveness of the economy – thus helping to cope with the crisis – through major infrastructure projects in the fields of transport (railway and inland waterway infrastructure), environment (treatment and disposal of solid waste, waste water), as well as support to SMEs.

2. POLITICAL CRITERIA

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

2.1. Democracy and the rule of law

Parliament

Parliament generally functioned well, fulfilling its constitutional role. However, there is scope for improving the level of parliamentary scrutiny in the legislative process.

The Administrative Court annulled in February 2009 parliament's controversial appointment of a Constitutional Court judge, ruling that the judge had not fulfilled the necessary professional requirements. The Constitutional Court subsequently overruled the Administrative Court decision such that parliament's appointment became final.

Parliament lifted the immunity from detention of a Member of Parliament convicted of war crimes charges. This was only after the first instance verdict was issued. However, the delay in taking the decision allowed the Member of Parliament to abscond the country once he had been sentenced and found guilty.

Government

The Government generally remained stable and continued to function normally, despite occasional political differences in the coalition, including the departure of the Pensioners' Party (one Member of Parliament) from the coalition in August, cabinet reshuffles and the appointment of a new Government under Prime Minister Jadranka Kosor following the resignation in July 2009 of the then Prime Minister Ivo Sanader.

In October 2008 the then Minister of the Interior and Minister of Justice, as well as the Head of Police, were all replaced. This was prompted by the killings of a lawyer and a journalist in Zagreb. The new ministers, who remained in the new Government after July 2009, are not members of ruling coalition parties and are considered experts in their fields.

Local elections were held in May, including for the first time direct elections of City Mayors and County Prefects. The elections were held in an orderly manner with an increased turnout.

Public administration

Some progress has been made on public administration reform, which is a key Accession Partnership priority. A new Law on General Administrative Procedures (LGAP) was adopted, aimed at supporting the establishment of service-oriented and professional administrative practice. Following the appointment of a new cabinet in July 2009, a new post of Minister for Administration was created. The capacity of the newly created Ministry of Administration (formerly the Central State Office for Administration) has further improved. Following the Amendments to the Civil Service Code of Ethics, the role and the responsibilities of the Ethics Committee and the competences of Ethics Commissioners were defined. The Government adopted a National Training

Strategy for Officials and Servants in Local and Regional Self-Government Units 2009-2013. It aims to improve the capacities of local self-government in providing decentralised services to citizens.

However, public administration reform has so far not received sufficient political attention. The appointment of a Minister for Administration provides an opportunity to inject the necessary political impetus into the reform process. Major weaknesses in administrative procedures remain and implementation of the new LGAP has not yet begun. The legal basis for building a modern and professional civil service is still incomplete. The draft Law on Civil Service Salaries has still not been adopted and a merit-based system of promotion and remuneration is missing. The civil service continues to suffer from many shortcomings, such as politicisation, low salaries (which fail to attract and retain sufficient numbers of qualified civil servants), lack of clear performance appraisal indicators, and weak human resources planning and management. Civil service salaries have been further cut to mitigate the effects of the financial crisis and a recruitment freeze introduced. Decision-making continues to be highly centralised with limited delegation of powers to middle and lower level management, leading to inefficiencies. The lack of an effective civil service registry still needs to be addressed. The law on the Ombudsman needs to be properly implemented so as to increase the effectiveness of the Ombudsman's recommendations. Anti-corruption measures and ethical principles remain to be embedded in public administration and the cooperation between different public stakeholders improved. With regard to the employment of national minorities, employment records in local and regional self-government units are not yet completed.

The Decentralisation Strategy has not been adopted, due to a lack of engagement at the political level. Overall coordination involving the line ministries at both political and technical levels is lacking, as is a dialogue among central and local governments. Training and improvement of the professional skills and knowledge of the Croatian authorities at central, regional and local level is not satisfactory.

Overall, some progress has been achieved in the area of public administration reform. Further efforts have to be made to substantially improve administrative procedures and to establish a professional, depoliticised civil service, able to fully respect the rule of law and with sufficient capacity to deliver quality services.

Following the appointment of a new Head of Police in October 2008 there were considerable changes in the staffing of the police, many of which were aimed at depoliticising key posts and improving professionalism. A number of persons in key positions were replaced, with the new appointments contributing to improvements at the managerial level. However, the Head of Police appointed in October 2008 was removed from his post in June 2009 and appointed as a State Secretary in the Ministry of Interior. Other key positions were also refilled. The reforms evident since October 2008 need to continue.

Civilian oversight of the security forces

Reform of the security and intelligence system has continued. With the necessary legislation in place and implemented, the intelligence services' conduct and scope of control has further improved. However, the legitimate interest of the State to protect certain information and the right of the public to have access to it are not yet properly balanced.

Overall, civilian control of the security services is generally assured.

Judicial system

Implementation of the **judicial reform** strategy has continued and a large volume of new legislation was adopted, in line with the key Accession Partnership priority in this area. The Ministry of Justice was reorganised and the directorate for strategic development reinforced. A new selection procedure for judicial trainees was introduced. The backlog of cases was reduced by 8.4% to 887,000 in December 2008. Good progress was made on reducing the number of old civil and criminal cases by 31% and 52% to 102,430 and 4,408 respectively. The new law on misdemeanours, the new civil procedure code, and the amended law on courts have contributed to reducing the inflow of new cases. New provisions of the criminal procedure code substantially modify the judicial investigation, transferring competence to the State Prosecutor. The new provisions apply from July 2009 for organised crime and corruption cases and as of 2011 for other cases. Special chambers for dealing with organised crime and corruption cases have been set up in four County Courts. Steps were taken to rationalise the court network. The number of municipal courts was formally reduced from 108 to 67 and the number of State Attorney's Offices from 71 to 55. The judicial academy continued to carry out its in-service professional training programme, and initial training programmes for judicial trainees and advisers started in April 2009.

However, the selection procedure for judges and prosecutors remains deficient, lacking transparency and the application of uniform, objective criteria. The overall case backlog and the number of unresolved cases older than three years remain high and the length of judicial procedures excessive. Problems with the enforcement of court rulings constitute a major obstacle to the efficiency of the judicial system. Court rationalisation has not yet begun in earnest, with very few physical mergers. Current plans lack ambition and clear budgeting. The draft law foreseeing the reduction in the number of misdemeanour courts from 114 to 61 has been pending approval in parliament for one year. There is still no unified statistical system of case management in the judiciary. Introduction of the integrated case management system is delayed. Further improvements in the accountability, independence, professionalism and competence of the judiciary are also required. The potential for undue political influence over the judiciary remains. The independence of the judiciary needs to be increased, and the role of the executive and parliament in issues such as judicial appointments reviewed. The judicial academy remains understaffed, without either permanent premises or an adequate budget to perform its duties. Initial training for future judges and prosecutors is still missing. The handling of administrative cases as well as the use of alternative dispute resolution continues to face particular challenges. Adequate monitoring of reform measures has not been possible due to continued limits on administrative capacity. There is only limited assessment of the impact of new measures.

With regard to domestic prosecutions for war crimes, Croatia continues to be active in trying war crimes cases on its own initiative, with around thirty trials in the past year. A more balanced approach is slowly becoming evident with a greater willingness to prosecute perpetrators irrespective of ethnicity. This is a key Accession Partnership priority. Further progress has been made on regional cooperation on war crimes matters. The State Attorney issued instructions to prosecutors in October 2008 aimed at addressing the problem of a common standard of criminal accountability for war crimes not being applied irrespective of ethnicity. The issue of *in absentia* verdicts from the 1990s has been partially addressed through an amendment to the criminal procedure code allowing wider possibilities to review cases.

However, impunity for war crimes remains a problem, especially where victims were ethnic Serbs or perpetrators were allegedly members of the Croatian armed forces. Many crimes remain unprosecuted, often due to a combination of lack of evidence, unwillingness of witnesses to come forward, e.g. due to intimidation, and unwillingness or reluctance of police and prosecutors, particularly in certain localities. There has been no further transfer of cases from local to specialised war crimes courts. Where cases are brought, judgments often take the convicted person's role in the

defence of the homeland as a mitigating factor, which creates a clear ethnic bias in sentencing for comparable crimes. There is so far only a limited track record of implementation of new review provisions for *in absentia* cases from the 1990s.

Overall, reforms in the judiciary continue but the impact of various newly introduced measures remains to be tested in practice. Significant challenges remain, particularly as regards judicial independence and the lack of transparent selection procedures for judges and prosecutors and as regards judicial efficiency, not least the length of proceedings and enforcement of decisions.

(See also Chapter 23 — Judiciary and fundamental rights)

Anti-corruption policy

There has been some progress in the fight against **corruption**. Implementation of the Anti-Corruption Strategy and related Action Plan has continued, which is a key Accession Partnership priority in this area. The legal framework to combat organised crime and corruption has been further improved. Amendments to the Criminal Code introduced new rules on confiscation of assets which reverse the burden of proof for persons convicted for organised crime or corruption offences. The National Council for monitoring the anti-corruption strategy has become more proactive, regularly holding public debates and hearings. A national anti-corruption campaign for the general public was launched. A National Police Office for the Fight Against Corruption and Organised Crime (PNUSKOK) has been operational within the General Police Directorate since February 2009. The Office for the Fight Against Corruption and Organised Crime (USKOK) continues to be active and has issued indictments in some important cases. It has begun to investigate possible high level corruption, initiating an investigation of a case involving a former government minister. There have been the first verdicts in some important cases brought by USKOK. In the second ‘Maestro’ trial, the Zagreb County Court issued prison sentences against two former vice-presidents of the Croatian Privatisation Fund (HFP).

However, corruption is still prevalent in many areas. The recently upgraded legal and administrative structures remain to be tested in practice. While the total number of corruption cases investigated so far has increased, the actual number of prosecutions remains low. There has been limited investigation of high-level corruption, the prosecution of which is frustrated by political influence. A culture of political accountability for the corruption being uncovered by USKOK is lacking. The administrative capacity of State bodies for fighting corruption continues to need improvement. Overall coordination of implementation of anti-corruption efforts still faces shortcomings. There has been no progress in preventing conflicts of interest. The Committee for the Prevention of Conflicts of Interest (CPCI) was re-established after a period of interruption but has not established a strong preventive role for itself. While this body has issued guidelines for State officials, there has been little progress in preventing conflicts of interest. Efficient non-partisan monitoring of anti-corruption efforts is still not established.

On the prosecution front, in order to be able to conduct complex financial investigations in the field of organised crime and corruption USKOK as well as PNUSKOK need to improve their expertise on financial issues as well as further enhance their cooperation with other bodies. In order to prevent corruption, greater transparency in public administration is required. Shortcomings remain as regards the financing of political parties and election campaigns. Implementation of the law on access to information needs further improvement. Public procurement remains a major source of corruption. Significantly improved scrutiny of actual execution of contracts is essential. *(See also Chapter 23 — Judiciary and fundamental rights)*

Overall, anti-corruption efforts continue and are producing initial results, but corruption remains prevalent in many areas and tools are not being deployed with sufficient vigour, especially on political corruption.

2.2. Human rights and the protection of minorities

Observance of international human rights law

There were no new **ratifications of human rights instruments**, as Croatia had ratified already in previous years most of the UN and Council of Europe core instruments. The Criminal Code has been amended with the aim of further aligning with the Council Framework Decision on combating Terrorism and the Council of Europe (CoE) Convention on suppression of Terrorism.

As of September 2009, there were 873 cases against Croatia pending before the **European Court of Human Rights** (ECtHR). The ECtHR delivered 19 judgments finding that Croatia had violated the European Human Rights Convention. As in previous years, the Court continued to find violations regarding the right to a fair trial and the length of the proceedings under Article 6 of the Convention. That has also increasingly encompassed the length of enforcement proceedings. The Court has also found violations of Article 13 — lack of an effective remedy in cases where local courts failed to issue verdicts following previous judgments on violations of the right to a fair hearing/length of proceedings by the Constitutional Court. The ECtHR concluded that in those particular cases remedies provided in the domestic legal system through recourse to the constitutional court were not effective.

The European Court of Human Rights has also condemned Croatia for different aspects of Article 6 regarding the dismissal of the former President of the Supreme Court of the Republic of Croatia. It has been established that the procedures before the State Judicial Council did not ensure the fairness of the proceedings.

The **promotion and enforcement of human rights** is often compromised by the overall shortcomings in the administration of justice. This relates especially to the length of proceedings in the judicial system.

Civil and political rights

With regard to **prevention of torture and ill-treatment and the fight against impunity** the Ombudsman continued to receive a number of complaints regarding the excessive use of force by the police. In this context, the Ombudsman repeatedly called for more transparent procedures for the determination of police responsibility as well as better regulation of police actions.

There has been no proper follow-up regarding the prominent case of forced hospitalisation reported on in the 2008 Progress Report.

As regards impunity, many war crimes are still unprosecuted, especially those where the victims are ethnic Serbs. According to the State Prosecutor, there are still some 600 cases to be investigated/prosecuted. In addition, there are several hundred cases which have yet to reach the Prosecutor due to lack of initial police investigation. Convicted persons are on occasion able to escape and shelter within the region due to dual citizenship and a lack of extradition agreements.

As regards **access to justice**, the Law on Legal Aid began to be implemented in February 2009. The necessary implementing legislation has been adopted and several legal NGOs have been registered with the Ministry of Justice. The institutional framework set up for implementation of the law

comprises a Department for Free Legal Aid within the Ministry of Justice, 20 State administration offices in counties and 13 branch offices as well as a Legal Aid Commission. However, the complexity of the procedure, low fees for lawyers relative to their normal tariffs and significant reductions in the budget for legal aid provision might not guarantee proper access to justice. Effective implementation of the free legal aid system is also jeopardised by the unequal territorial distribution of NGO legal providers.

With regard to the **prison system**, further measures have been taken to improve prison conditions, in particular the management of the prison system. The Law on enforcement of prison terms was adopted in 2008, providing for the expansion of existing facilities and improved health care. 171 additional staff were recruited and trained. However, Croatian prisons remain overcrowded, with the number of detainees increasing due to longer prison sentences introduced in the Criminal Code. Probation remains to be introduced as an alternative to detention. There is still a lack of trained prison staff. There have been cases of abuse of office and corruption among prison staff that have favoured certain prisoners. First efforts have been made to address this issue.

Freedom of expression, including freedom and pluralism of the media, is provided for in Croatian law and is generally respected. However, threats against journalists working on cases of corruption and organised crime have been increasing. There has been limited success in identifying and prosecuting perpetrators and instigators of certain physical attacks on journalists. Editors and journalists continue to report undue political pressure. Concerns about freedom of expression persist, including at the local level.

There have been no particular difficulties as regards **freedom of assembly and association**.

Civil society organisations play an important role in the promotion and protection of human rights, democracy and protection of minorities. However, they continue to have difficulty influencing policy debate, partly due to the government tending not to include them in the policy-making process. With a few notable exceptions, NGOs remain relatively weak in analytical capacity.

There have been no particular problems in the exercise of **freedom of religion**.

Overall, with some specific exceptions, civil and political rights continue to be reasonably well respected in Croatia. However, shortcomings as regards impunity for war crimes, access to justice and freedom of expression require further attention.

Economic and social rights

There has been some progress in the area of **women's rights** and gender equality.

Implementation of the new Gender Equality Act and of the national policy for the promotion of gender equality continued. Implementation of the national strategy for protection against domestic violence 2008-2010 has improved. There has been further progress in police work in cases of family violence. The Ombudsman for Gender Equality makes use of all available instruments and reports by public bodies and enterprises respond in a satisfactory manner. There has been good cooperation between the authorities and the Ombudsman, especially on the new anti-discrimination legislation. The political participation of women improved following the local elections held in May 2009.

However, the situation of women on the labour market remained unchanged. Women are affected disproportionately by the widespread use of fixed term contracts. This discourages them from complaining about discrimination. The professionalism of social welfare centres and staff training in cases of domestic violence needs further improvement. Despite provisions of the Gender Equality

Act requiring all public administration bodies, at the central, local and regional level, as well as other institutions to collect, process and present data disaggregated by gender, such data is still missing.

(see also Chapter 19)

There has been little progress in the area of **children's rights**. The Ombudsman for Children continued to be effective in his role in the overall promotion and protection of children's rights. In 2008, the Ombudsman for Children dealt with 2,075 new cases. He noted a small decrease in reports of violence in the family. There has been good cooperation between the authorities and the ombudsman, especially on the new anti-discrimination legislation. A National Programme for Young People 2009-2013 has been adopted.

However, violence among and against children in educational institutions has increased. Social welfare institutions and correctional facilities remain understaffed and overburdened. The number of children in institutions has increased. Implementation of measures envisaged under the national plan of activities for the rights and interests of children for the period of 2006-2012 has been further delayed. There is poor coordination between ministries with regard to children's rights. Judicial backlogs and the lack of trained judges have a negative impact on the situation of children, particularly in cases of family separation and in unpaid alimony cases. Amendments to the family law from 2007 have not produced the expected results in terms of reducing the non-payment of alimony.

Progress has been good in the area of **socially vulnerable and persons with disabilities**.

The Office of the Ombudsman for Persons with Disabilities (OPD) was inaugurated in November 2008 and was adequately staffed in April 2009. The OPD has been successful in carving out a visible role for itself. Public bodies and private enterprises are responsive to recommendations received by the OPD. A good indicator for concrete improvement is that today, almost all new buildings under construction take into account the need for accessibility of the building to disabled persons. The office in practice deals more with requests for information than with individual complaints. The media have been very cooperative in disseminating awareness-raising information. There has been good cooperation between the authorities and the ombudsman, especially on the new anti-discrimination legislation.

However, more progress is needed in the field of de-institutionalisation, including for children with disabilities. This is among the priorities set out in the Joint Inclusion Memorandum (JIM) and the related National Implementation Plan. Despite the provisions of the JIM, data on exclusion is still missing. Civil society organisations involved in delivering community-based services need to be adequately supported in order to develop sufficiently community-based services as an alternative to institutionalisation. In general, serious inadequacies in the social welfare system remain. *(see also Chapter 19 – Social policy and employment)*

With regard to **labour and trade union rights**, there has been some progress *(see also Chapter 19 – Social policy and employment)*. Against a challenging economic background, the trade unions are increasingly gaining the ability to influence government policy and decision making. However, the monitoring and follow-up by the State Inspectorate and the judicial system of violations of workers' rights remains weak.

The new **anti-discrimination** law is in an early phase of implementation. The Ombudsman has started to exercise his new responsibilities. However, proper implementation of the new law is jeopardised by recent budget cuts. Discrimination against minorities remains a particular problem

(see below). There has been no progress with implementation of hate crime legislation. There has been no conviction for the criminal offence of the initiation of racial and other hatred. More needs to be done to tackle discrimination on grounds of sexual orientation. Lesbian, gay, bisexual and transgender people are subjected to threats and attacks. Many cases are not followed-up adequately by the police and prosecutors, or remain unreported.

The level of protection against discrimination in practice and the judicial prosecution of acts of discrimination is not in line with EU standards.

Property rights are generally assured. The outstanding cases of delayed property repossessions and problems with compensation for the use of private property taken under the war legislation from the 1990s continue to be present.

Overall, legal protection for economic and social rights is partially guaranteed. Implementation of women's and children's rights and protection against all forms of discrimination needs to be further improved in practice.

Minority rights, cultural rights and protection of minorities

There has been some progress in the area of **minority rights, cultural rights and protection of minorities**.

High-level public expressions of commitment to the rights of minorities, reaffirming their place in Croatian society, have continued. The eight minority MPs are in the governing coalition. The Roma minority has continued to receive attention, with improvements particularly in pre-school education. Round tables and public discussions have been held on the constitutional law on the rights of national minorities (CLRNM), in particular concerning minority employment in the State administration and judiciary. With regard to cultural rights, the education provisions of the CLRNM and other laws relevant to minorities generally continue to be implemented satisfactorily. With regard to the perception of national minorities in the media, negative stereotyping has further decreased.

However, many problems remain for minorities. Minorities continue to face particular difficulties in the area of employment, both in terms of under-representation in the State administration, the judiciary and the police as well as in the wider public sector. Limited progress has been made with regard to the implementation of the CLRNM, which is a key Accession Partnership priority. The implementation of the recruitment plan for national minorities has not seen a significant increase in minority employment in the State administration. Plans for employment in the administration at county, town and municipality level are still not adequate. A long-term strategy to implement the CLRNM minority employment provisions is lacking. Adequate statistics to allow proper monitoring are not available.

Despite increased financial support, the Councils for National Minorities (CNMs) are not sufficiently recognised yet as advisory bodies by the majority of local authorities. Moreover, their independence and influence is affected by the fact that they depend on the budget of the town authority or council.

Legal provisions and programmes need to be implemented with more determination, and adequate monitoring assured, especially in the area of employment. There continues to be little progress with regard to the production and/or broadcasting of programmes for minorities in their languages by public radio and TV stations, as envisaged under the CLRNM.

With regard to the **Serb minority**, there have been fewer reports of ethnically motivated attacks. Police investigations of such incidents have improved, although few cases end in prosecution. Many cases remain unreported due to a lack of confidence in the authorities and the occurrence of negative sentiment in the wider public towards Serbs. Members of the Serb minority, including those who remained in Croatia during the war, face difficulties concerning access to employment, especially in the war-affected areas. Discrimination continues, particularly in the public sector at the local level. Croatia needs to encourage a spirit of tolerance towards the Serb minority and take appropriate measures to protect those who may still be subject to threats or acts of discrimination, hostility or violence.

There has been some progress on the various outstanding issues regarding **refugees**.

Around 1,345 refugees and 380 displaced persons returned to their place of origin in Croatia in 2008-2009. The total number of Serb minority returns to Croatia now stands at 108,466 in addition to 23,231 internally displaced Serbs who have returned to their home towns and villages. There has been progress in providing housing solutions to returning refugees. The programme to reconnect public infrastructure in certain return villages and mine clearance operations have continued. Despite significant progress in recent years in the area of return and (re)integration in the signatory countries of the Sarajevo Declaration, a total of some 80,000 Croatian Serbs are still registered as refugees in the region, the vast majority in Serbia.

A number of obstacles to sustainable return of Serb refugees remain, the main one being housing, particularly for former tenancy rights holders. Implementation of the Croatian government's housing care programmes (HCP) within and outside the Areas of Special State Concern (ASSC) for former tenancy rights holders who wish to return to Croatia has progressed well over the past year but is lagging behind the planned timetable. Definitively settling all cases in this area is a key Accession Partnership priority.

In total, as of September 2009, 13,695 HCP applications had been filed. Out of this number 8,888 had been positively decided, of which 6,198 cases had received housing assistance. 2,567 cases were decided negatively, resulting in some 686 appeals. 2,240 cases were not yet completed.

In terms of government planning for the allocation of apartments under the HCP, implementation of the self-imposed benchmark for 2007 (allocating 1,400 housing units) has been met. As for the 2008 benchmark (an additional 1,400 housing units) good progress has been made, with more than three quarters of cases having been finally resolved. In addition, many cases have been transferred to reconstruction schemes, with contracts for organised reconstruction signed, though implementation is not yet complete. The government has reduced its objective for 2009 from 2,496 to 2,100 housing units, due in part to postponed or cancelled applications. Implementation is at an early stage. In addition to the pending cases from the 2008 and 2009 benchmarks, it is estimated that anywhere up to 2,000 housing units will need to be provided in 2010 and possibly beyond to returning refugee families under the HCP. Figures will, however, depend on the results of processing the 2-3,000 pending requests and appeals, on the number of new applications and on the number of cases to be transferred from the reconstruction scheme to the housing care programme. Croatia should ensure that budget cuts necessary in the context of the economic crisis do not weigh negatively on refugee return issues.

Reconstruction of housing has continued. However, around 8,000 appeals are still pending, most of which for more than four years. Property repossession is largely complete. There has been progress in returning previously occupied agricultural land plots to the pre-war possessors and rightful owners.

Apart from housing, other key concerns facing returnees are employment, enduring hostility in certain localities and ‘convalidation’, or the validation of working years for the purpose of pension rights, of those residing in the parts of Croatia not under Croatian government control during the 1990s. Lodged claims for convalidation amount to 17,586. Of this number, 9,610 have been processed, with 52% receiving a positive decision. The decision to revise all negative decisions in an internal audit is a positive development; nevertheless, measures aimed at ensuring a more uniform and fair application process notably at the first instance level should continue.

Good progress has been made as regards inclusion of the **Roma** minority, building upon the willingness of Croatia to address the problems of this group. It has launched a number of infrastructure programmes with EU financial support in Roma settlements. There has been progress as regards enrolment of Roma children in pre-school, as well as primary and secondary education. Funding for Roma projects is also increasing. Some special language classes which resulted in de facto segregation of Roma children have been integrated into mainstream programmes.

However, most Roma remain excluded from mainstream Croatian society and face difficult living conditions. Unemployment remains endemic. Measures with regard to education need to be integrated into more systematic policies. Progress on successful completion of primary and secondary education is relatively modest so far. Problems persist also in terms of access to employment, adequate housing, social protection and healthcare, and in general attitudes in society, where discriminatory viewpoints prevail. Coordination among Roma groups is limited as is their expertise for effective implementation, and should be strengthened. The lack of personal documents and/or civil registration continues to hinder the integration of Roma into existing communities and their access to employment, health and other rights. Problems remain regarding the participation of the Roma community in the education system, even when specific programmes are available.

Overall, the position of minorities in Croatia continues to improve. However, many problems remain for the Serb and Roma minorities. Some progress on outstanding refugee return issues was made but efforts to provide housing solutions and ensure sustainability of refugee return need to be accelerated.

(See also Chapter 23 — Judiciary and fundamental rights)

2.3. Regional issues and international obligations

Compliance with the **Dayton/Paris and Erdut Peace Agreements** has overall been ensured.

Croatia continues to cooperate with **the International Criminal Tribunal for the former Yugoslavia (ICTY)**. This is a key Accession Partnership priority. However, problems of access for ICTY to important documents in Croatia continue to exist. These documents are required in the ongoing ICTY trial against generals Gotovina, Cermak and Markac. Subsequent to an order of the Trial Chamber of September 2008, Croatia was required to provide a detailed report specifying the efforts undertaken to obtain the requested documents. However, in his June address to the Security Council, the ICTY Chief Prosecutor stated that *progress in Croatia’s investigation into the fate of the missing documents had been limited and that the large majority of the military documents sought had not been submitted to the Tribunal*. In the same month, Croatia submitted a motion requesting the Trial Chamber to decide whether Croatia had complied with its order of September 2008. Croatia needs to ensure all necessary steps are taken to settle this issue.

There has been improved cooperation regarding the exchange of evidence and the transfer of some war crimes cases between the prosecutors from Croatia, Bosnia and Herzegovina and Serbia. Obstacles to the extradition of suspects in cases of war crimes and crimes against humanity between

the countries of the region continue to exist, however. This exacerbates the problem of impunity, as has been demonstrated in one high-profile case where a convicted war criminal was able to escape from Croatia to Bosnia and Herzegovina on the basis of having previously acquired citizenship of the latter from where he cannot be extradited. As regards the possibility of serving the sentence in Bosnia and Herzegovina, the existing agreement on mutual recognition of sentences requires the convicted person's consent for the sentencing to be served in the other countries. Croatia, together with its neighbours, should address the regional impunity gap, including by taking steps towards extradition agreements covering war crimes cases.

Croatia's policy regarding the **International Criminal Court (ICC)** is aligned with the EU Common Positions on the integrity of the Rome Statute as well as related EU guiding principles.

There has been little progress in the **Sarajevo declaration** process, which aimed to finalise the regional refugee return process by the end of 2006. While Croatia continued to work on its roadmap, there has been limited discussion on implementation issues on either a bilateral or a regional basis. Further efforts are needed to resolve the main outstanding issue not yet addressed, namely how to deal with the compensation claims of those who lost occupancy and tenancy rights in Croatia.

Regional cooperation and good neighbourly relations form an essential part of the process of moving towards the European Union. Croatia continued to participate actively in regional initiatives, including the South-East European Cooperation Process (SEECP), the Regional Cooperation Council (RCC), the Central European Free Trade Agreement (CEFTA), the Energy Community Treaty and the Agreement on the European Common Aviation Area (ECAA). Croatia joined the North Atlantic Treaty Organisation (NATO) in April 2009.

Bilateral relations with other enlargement countries and neighbouring EU Member States continue to develop. However, progress towards finding definitive solutions to various open bilateral issues between Croatia and its neighbours, particularly as regards settlement of border disputes, has been uneven. This is a key Accession Partnership priority. There has been some progress towards reconciliation among citizens in the region, which is also a key Accession Partnership priority. More needs to be done to pursue efforts in this area.

Croatia continues to have good relations with *Albania* and *the former Yugoslav Republic of Macedonia*.

Bilateral relations with *Bosnia and Herzegovina* remain stable. However, relations have been burdened by various trade disputes, in particular following the imposition by Bosnia and Herzegovina of import restrictions on agricultural products which are contrary to CEFTA obligations. There has been no progress on border issues. Ratification of the 2005 Agreement on Demarcation of the Land and River Borders remains on hold. Moreover, the dispute over two islands – Veliki Skoj and Mali Skoj – remains unresolved, as does the issue of the border along the River Una. The Peljesac bridge project remains an open political issue. There have been no developments on the agreement on the use of the Port of Ploče. The Interstate Cooperation Council has not met over the reporting period. Other unresolved issues include property and refugees.

Relations with *Montenegro* have continued to improve. Progress has been achieved towards settling the bilateral border issue concerning Prevlaka and both countries have been co-operating on preparing their submission to the International Court of Justice. An agreement on the protection of minorities was signed. The temporary border regime in place continues to function smoothly. The

joint working group on resolving property issues and the council on economic relations both held meetings. An agreement on cooperation in science and technology was signed.

There has been progress in relations with *Serbia*, in particular following the visit of the Croatian Prime Minister to Belgrade in March 2009. There have been several other senior bilateral meetings. The Serbian Ambassador, recalled after Croatia recognised the independence of Kosovo³, returned in November 2008. The visa-free arrangement between the two countries continues to function well. Croatia and Serbia signed an agreement on police cooperation, an agreement on readmission of illegal migrants and on cooperation in the field of European integration. There has been some progress in cooperation on the 2,000 cases of missing persons from the war. However, there has been no progress towards a border agreement, nor has the bilateral commission met. Other open matters include property-related issues, in particular claims for compensation for lost occupancy and tenancy rights, refugee return and the genocide lawsuits before the International Court of Justice. Relations were particularly strained amid harsh rhetoric from both sides concerning the ICJ case at the end of 2008. Economic cooperation is growing although there are limited Serbian investments in Croatia compared to the level of Croatian investments in Serbia, possibly due in part to reluctance in Croatia to accept Serbian investments.

Croatia continues to have good relations with *Hungary* and *Italy*.

Relations with *Slovenia* have been affected by the outstanding border issue. The border issue between the two countries held back the accession negotiations such that a substantial number of chapters could not be opened or closed until October 2009, although technically finalised earlier. The Commission has provided its facilitation services to settle this dispute. Intensive efforts by the Commission, supported by the Trio of Presidencies, have been made over six months, which paved the way for a political agreement between the two parties reached in September 2009. There has been no progress in resolving the open issues concerning the Ljubljanska Banka/SFRY Succession Agreement (guarantee of foreign currency deposits).

Overall, Croatia continues to cooperate with ICTY, although problems concerning access to important documents persist. Croatia continues to participate actively in regional cooperation. Good neighbourly relations have prevailed, although there are shortcomings on addressing outstanding issues, especially concerning the settlement of border disputes, property issues and refugee return.

3. ECONOMIC CRITERIA

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

3.1. The existence of a functioning market economy

Economic policy essentials

The country participates in the EU Pre-Accession Fiscal Surveillance procedure. The Pre-accession Economic Programme (PEP) 2009-2011, submitted in January 2009, presented a sufficiently comprehensive and consistent macroeconomic and fiscal framework for economic policies. The

³ Under UNSCR 1244/99.

programme and its assumptions became however quickly outdated due to the impact of the international crisis. The fiscal notification submitted in April 2009 was an important step in further aligning fiscal reporting to ESA 95 standards, although weaknesses remain. Broad political consensus on the key essentials of a market economy has been maintained. Transparency on economic policy issues and in decision making was improved by the setting-up of an economic council comprising major stakeholders. However, economic policy making was often based on ad hoc decisions and economic reforms sometimes lacked a strategic medium-term orientation. *Overall*, consensus on the fundamentals of a market economy has been maintained, but Croatia lacks a medium-term and structural reform strategy.

Macroeconomic stability

The global financial and economic crisis started to affect the Croatian economy more severely in the last quarter of 2008, when GDP growth dropped markedly to 0.2% year-on-year. For the whole year of 2008, annual GDP growth slowed to 2.4%, down from 5.5% in 2007. In particular, private and public consumption growth slowed considerably in the course of 2008, while real investment growth accelerated (from 6.5% in 2007 to 8.2% in 2008), mainly on the back of strong activity in non-housing construction. The growth of exports declined to 1.7% (from 4.3% in 2007), while total imports decelerated to 3.6% (6.5%), and the contribution of net exports to growth remained negative. On the supply side, growth was mainly driven by the still robust performance of some services, including financial intermediation, construction and transport. Economic performance deteriorated significantly in the first half of 2009. Real GDP declined by 6.5% year-on-year, on the back of sharp drops in private consumption (-9.7% year-on-year) and investments (-12.6%). Industrial production declined by 9.1% year-on-year in July, indicating further drops in output in the third quarter. At the same time the tourism sector performed better than expected during summer, somewhat cushioning the recession. Average per-capita income in 2008 rose to 63% of the EU-27 average, from 61.1% a year before. *Overall*, the global crisis has led to a significant economic downturn.

In 2008, the current account deficit widened to 9.4% of GDP, up from 7.6% in 2007. This was partly driven by a deterioration of the trade balance. Higher oil prices and declining growth of exports to the main trading partners in the EU pushed the trade deficit up to 22.9% of GDP, from 22% a year before. As in previous years, roughly two thirds of the trade gap was covered by the surplus in services, mainly tourism and transport. The deficit of the income balance increased markedly, from 2.6% in 2007 to 3.3% in 2008, mainly reflecting higher debt servicing costs in an environment of tighter external financing constraints and lower foreign revenues. In the first seven months of 2009, the trade and current account deficits gradually declined, as merchandise imports dropped more strongly (-26.8% year-on-year) than exports (-20.7%). In the twelve months to June 2009, the current account deficit shrank to 6% of GDP. *Overall*, the current account deficit has been declining in line with slowing domestic demand.

While net capital inflows remained relatively strong in the first three quarters of 2008, they came to a temporary halt during the last quarter. For the year as a whole, they reached 11.6% of GDP (somewhat higher than in 2007) and were again largely driven by foreign borrowing of banks and companies. In the context of tighter external financing conditions in late 2008, even some temporary capital outflows occurred, as private agents increased their foreign currency deposits abroad. Private banks started drawing down their external reserves to increase their foreign financing and to service outstanding external obligations. In the first half of 2009, total net capital inflows halved compared to the same period a year before. Net FDI remained an important source of foreign financing, although net inflows fell from 8.7% of GDP in the first half of 2008 to 3.9% of GDP in the first half of 2009. Net FDI covered around one third of the current account deficit,

compared to 45% in the same period a year before. The structure of FDI continued to be dominated by equity investments, including moderate recapitalisations in the banking sector as well as the takeover of parts of the domestic oil company. *Overall*, despite slower net capital inflows due to the crisis, a sufficient amount of external financing could still be ensured.

The heavy external debt burden continued to increase, by €5.9 billion in 2008, and a further €1.6 billion in the first half of 2009. At end-2008, the stock of debt amounted to €39.1 billion, equivalent to around 82.6% of GDP, up from 77.6% at end-2007. The rise in external indebtedness was mainly due to intensive corporate sector borrowing which slowed however in late 2008 as a consequence of the crisis. Domestic banks managed to secure the roll-over of liabilities vis-à-vis parent banks in the last quarter of 2008, and increased their external debt in 2009. The relatively large exposure of the domestic non-tradable corporate sector, which accounts for around 40% of gross foreign debt, remains a cause for concern and warrants careful monitoring. A high external debt level, large exposure of the non-tradable sector and large debt obligations maturing over the short term continue to represent key external vulnerabilities of the Croatian economy.

According to data from the labour force survey, the unemployment rate further declined from 9.6% in 2007 to 8.4% in 2008. In the first quarter, it stood at 9.4%, compared to 10% a year ago. However, registered data confirm that the economic downturn has already taken its toll on the labour market. Total employment declined by 3.7% in the twelve months to July 2009. In the same period, the officially registered unemployment rate rose from 12.2% to 14%. Moreover, the Croatian labour market continues to suffer from structural problems, such as low participation and employment rates as well as high rates of youth and long-term unemployment. The effective retirement age remained low and significant labour supply disincentives persisted, such as generous early retirement rules and the predominance of categorical social welfare benefits. Stronger labour demand remained hampered by relatively rigid employment protection systems. As a result, labour turnover remained low, suggesting limited employment restructuring. The growth of average gross wages accelerated to 7.1% in 2008, up from 6.2% in 2007, and declined to 4% in the first half of 2009. Average real wage growth picked up somewhat recently, as inflation started to subside. *Overall*, labour market performance deteriorated as a result of the crisis and major structural weaknesses persist.

The monetary and foreign exchange system of a tightly managed float with a very limited degree of exchange rate flexibility remained in place as a main device to anchor inflation expectations. It has also helped mitigate potential exchange rate-induced credit risks in a highly euroised economy. Under conditions of a less benign external environment, tighter external financing constraints and higher lending spreads, the central bank released significant foreign exchange liquidity to the domestic banking system through a set of subsequent measures. This included the abolition of marginal reserve requirements on banks' foreign borrowing as well as a relaxation of reserve and liquidity requirements, effectively unfreezing banks' foreign currency holdings. Moreover, the central bank intervened twice in the foreign exchange market by selling euros for a total amount of around € 513 million⁴. As a result of monetary policy measures, official foreign reserves, which stood at € 9.3 billion at end-2007, started to drop in the second half of 2008. They temporarily fell to € 8.6 billion in February 2009, and recovered to €9.1 billion by June, equivalent to around 5 months of imports. The average daily exchange rate fluctuated within a relatively small range between 7.11 and 7.49 kuna per euro and depreciated by 3.1% between October 2008 and mid-

⁴ Following those two interventions, the central bank bought euros in a third intervention to mitigate appreciation pressures.

September 2009. *Overall*, monetary policy has managed to relieve external financing pressures by regulatory measures and thus contributed to preserving stability.

The current monetary framework required a relatively tight monetary stance, directed at limiting domestic kuna liquidity in line with available foreign exchange resources in order to ensure exchange rate and financial stability. Open market operations (repo auctions) were undertaken at a set rate of 6%, which effectively led to rationing, weaker market transparency and an increase in market rate volatility. Moreover, to allow for a more restrictive policy stance during periods of elevated depreciation pressures the authorities tightened collateral requirements. Domestic monetary and credit aggregates have been largely affected by the financial crisis, the economic slowdown and the monetary policy response. Annual growth of domestic credit to the private sector further decelerated from around 15% in 2007, but was still around 10% in 2008 and 4.3% in July 2009. In particular, the growth of lending to private households dropped more strongly than lending to the corporate sector. Domestic firms have increasingly shifted towards domestic sources of financing as a reaction to lower and more costly access to foreign capital. At the same time, the structure of outstanding credit has changed markedly due to a strong increase in government borrowing since December 2008. *Overall*, credit growth has fallen and the structure of credit has shifted towards government financing.

In 2008, average annual inflation increased significantly to 6.2%, up from 2.9% in 2007. This resulted from strong increases in oil and food prices in the first seven months and large carry-over effects from 2007. Following its peak in July 2008, annual inflation declined to 2.8% at end-2008 with lower energy and commodity prices and a slowdown in economic activity and private consumption growth. During the first quarter of 2009, inflation picked up temporarily to 3.8%, mainly resulting from adjustments in regulated gas prices, an increase in excise duties on tobacco and a seasonal increase in vegetable prices. In August, annual inflation came down to 1.4%. Core inflation decelerated to 4.1% at end-2008 and further to 3.4% in mid-2009. *Overall*, as a result of falling world prices of commodities annual inflation has come down from its peak in 2008 with some temporary upward pressures in early 2009 mainly due to adjustments in regulated prices.

Public finances have come under increasing pressure since the fourth quarter of 2008, when revenues started to underperform in line with a deceleration of economic activity. The authorities reacted swiftly by adjusting current spending at short notice in the last months of 2008, and thereby managed to maintain the general government deficit for the year as a whole at 1.4% of GDP. However, revenue performance continued to weaken significantly in early 2009, forcing the government to increase domestic borrowing. The budget financing situation was temporarily alleviated by a successful € 750 million government eurobond issue in May. In the first half of 2009, state budget revenues declined by 8.6% year-on-year while expenditures increased by 7.9%. The central budget balance turned into a deficit, equivalent to 2.2% of projected GDP, compared to a surplus in the same period a year before. A bleaker economic outlook and worsening fiscal trends led the authorities to adopt a series of budget revisions. The first revision in April included a wage freeze for civil servants and public employees; it was however still based on optimistic growth assumptions. Considerable risks to the 2009 budget execution materialised quickly. A stronger-than-expected economic downturn and rapidly falling revenues forced the authorities to adopt a second, and shortly thereafter a third budget revision, in early and mid-July, respectively. The revisions included some cuts on spending and a number of measures to compensate for falling revenues, such as a special tax on income, a VAT increase of one percentage point, and increases in excises. Despite those adjustments, the revised planned general government deficit increased to 3.3% of GDP, thus pushing up financing requirements of the government sector and related financing risks. Moreover, risks of further declining revenues and higher spending aiming at combating the current crisis remained high. The stock of general government debt stood at 33.5% of

GDP at end-2008, only slightly higher than a year before (33.1% of GDP), but it went up considerably in the first half of 2009. Adjustments for the stock of issued state guarantees and the debt of the State Development Bank (HBOR) would raise the stock of debt by around 10 percentage points of GDP. *Overall*, in reaction to mounting fiscal pressures, efforts were made to re-balance the budget. However, the policy response came late, revealing weaknesses in budget planning, and the fiscal deficit increased significantly.

The rationalisation of public spending has made limited progress. This is a key Accession Partnership priority. Some health reform measures were enacted as an important step towards addressing the sector's financial difficulties, including a more effective system of co-payments. No further reforms have been undertaken to achieve better targeting of social support, as envisaged under the social benefits reform strategy adopted back in 2007. Categorical benefits still account for the large majority of social spending. There has been no progress on reforming the mandatory pension system. *Overall*, apart from important initial health care financing reforms, little progress has been achieved in terms of increasing the efficiency of public spending.

The implementation of a comprehensive treasury reform strategy has continued with a view to further improving expenditure management and budget control systems. A new Budget Act came into effect, improving the legal basis for strategic and multi-annual budget planning. Continued progress was achieved in enhancing institutional and analytical capacity for setting up medium-term macroeconomic and fiscal frameworks. However, further progress in streamlining procedures would be needed to more effectively link defined policy priorities to the budget planning process. Further substantial efforts were undertaken to bring budget reporting more in line with ESA 95 standards. Fiscal transparency remains a concern, also due to the non-inclusion in the general government accounts of some quasi-fiscal operations (State Development Bank, Motorway Company) and a large number of municipalities. *Overall*, analytical and institutional capacity in public finance has improved, but strategy-based budget planning needs to be further strengthened.

Overall, the macroeconomic policy response has by and large been appropriate to address the spill-overs from the global economic and financial crisis. Within its given limits that ensue from the high degree of euroisation, monetary policy contributed successfully to preserving financial stability mainly through regulatory changes alleviating foreign exchange liquidity pressures. In reaction to mounting fiscal pressures, efforts were made to re-balance the budget. However, the gradual deterioration of the fiscal balance in combination with tight financing would have required a somewhat more timely and comprehensive fiscal response. The design of a credible fiscal strategy aimed at reducing budget rigidities and enhancing the efficiency of public spending remains a key challenge.

Interplay of market forces

The privatisation process progressed slowly. The only major transaction was the sale of additional assets of the national oil company to a foreign investor. The privatisation of assets held under the State Privatisation Fund made only limited progress. Up until June 2009, the State Privatisation Fund had sold or liquidated shares in some 103 companies, mainly consisting of minority shares. A total number of 29 tenders were published for the privatisation of companies in majority state ownership, but only 4 companies were actually sold. A number of issued tenders have not been successful, partly due to a lack of interest among potential investors and, in some cases, rather unrealistic sale conditions. The remaining portfolio of the Privatisation Fund still comprised 835 companies, with the State keeping a majority holding in 85 of them. Thus, the portfolio of the Fund has virtually remained unchanged. No progress has been achieved with the implementation of a new privatisation model under which state assets would be transferred to investment funds. The private

sector's share in employment has remained at around 70%; the private sector share of GDP is estimated at around 70-80%. *Overall*, very limited progress has been achieved in reducing the role of the State in the real sector of the economy.

Market entry and exit

Company registration procedures have been further simplified, also by the introduction of on-line registration for limited liability companies. Preliminary data indicate that the number of newly registered companies declined by 27%⁵ and the stock of active businesses increased by 5.4% year-on-year in June, compared to a growth rate of 8% a year before. The government's project to reduce the regulatory burden by streamlining legislation and eliminating unnecessary regulations ('regulatory guillotine') started off well in 2007, but its implementation slowed. The investment climate remains hampered by difficulties in obtaining necessary licences, building permits and other authorisations. A large number of para-fiscal taxes at the national and local level do seem to add significantly to the tax burden of entrepreneurs. The business environment is also affected by petty corruption and an inefficient public administration. *Overall*, further progress has been made in simplifying company registration, but the investment climate continued to suffer from a heavy regulatory burden and numerous para-fiscal taxes. Improving the business environment is a key Accession Partnership priority.

Legal system

Further progress was made in reducing the backlog of cases before Croatian courts. During 2008, the backlog was reduced by 8.4% compared to 2007. However, there is still a large backlog (887,000 cases at end-2008). The length of proceedings before the courts remains generally excessive and major problems continue to exist with the enforcement of court decisions. The weaknesses of the judicial system continue to undermine effective enforcement of creditor and property rights. Land registration has improved, but remains incomplete in parts of the country. Investors still suffer from lengthy procedures to register a property. *Overall*, improvements to the judicial system have been made, but major inefficiencies in the judiciary remain.

Financial sector development

The financial sector remained dominated by banks, representing around 77% of total assets of financial intermediaries in mid-2009. The banking sector is almost completely privatised with a 90% share of foreign ownership in terms of net assets. Out of 33 banks, two banks remained state-owned. The degree of market concentration has remained at a moderate level and has generally not been an impediment to market competition. The four largest banks together kept a market share of around 65% by mid-2009. Banking sector assets continued to grow, but at a slower pace, and the structure of assets changed considerably. This is due to a reduction of banks' foreign assets and reserves with the central bank, resulting from regulatory changes. Total credit growth slowed, reflecting lower demand and higher risk awareness of banks in the context of the global financial crisis, but lending to the government sector increased strongly. In terms of GDP, total bank lending continued to rise, from 68.8% in 2007 to 72% of GDP in 2008, and further to 74.6% in mid-2009. *Overall*, the largely private and foreign-owned banking sector remained the key financial sector player with a moderate degree of market concentration.

As a result of a number of prudential and supervisory measures that had been taken earlier to address potential macro-financial vulnerabilities, the banking sector remained well capitalised, and

⁵ Last quarter 2008 and first half of 2009 compared to the same period a year earlier.

profitability indicators stayed at rather comfortable levels in 2008, before they slightly worsened in the first half of 2009. The share of non-performing loans increased from 4.9% at end-2008 to 6.1% in June 2009 under a less favourable economic environment. Moreover, the banking system remained confronted with considerable interest- and currency-induced credit risks, as the majority of loans are based on variable interest rates and denominated in or indexed to foreign exchange. Financial sector stability developments have been kept under close watch by the central bank, which further enhanced its institutional and analytical capacity to produce forward-looking financial sector stability assessments of high quality. *Overall*, the banking sector remained resilient to shocks, but significant risks are related to largely un-hedged balances of the non-financial private sector.

The share of non-banking financial sector assets in total financial sector assets declined from 26% at end-2007 to 23% in mid-2009, largely due to poor performance of investment funds, which experienced significant share price declines and money withdrawals in the context of the global financial crisis. At the same time, leasing companies and the insurance sector gained in absolute and relative terms. The domestic stock and bond markets also suffered from the deepening international crisis. The stock market index lost almost 70% in 2008, and market capitalisation of shares listed on the Zagreb stock exchange fell from 128% to 42% of GDP. Stock markets started to recover somewhat in March 2009, and the index gained some 15% in the first half of the year. In 2008, bond markets registered the lowest turnover since 2003, and market capitalisation of all listed bonds declined from 15% to 10% of GDP, resulting from falling bond prices, maturing bonds and limited new bond issues. *Overall*, notwithstanding the growth of some market segments, financial intermediation by the non-banking sector remained shallow and stock and bond markets experienced significant losses following the outbreak of the crisis.

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

Existence of a functioning market economy

The policy response to the global financial crisis has by and large been conducive to preserving macro-financial stability, although fiscal risks remain significant. A prudent response by monetary authorities as well as efforts to re-balance the budget helped anchor expectations of economic agents and supported the functioning of market mechanisms. However, the slow pace of economic restructuring and prevailing obstacles to private sector development continued to partly undermine a more growth-oriented allocation of resources, constraining the potential for higher productivity and catching-up over the medium term.

Human and physical capital

Reforms in the education sector have continued under the education system development plan for 2005-2010. Further steps were taken to improve the quality of education at all levels, including through the provision of educational programmes for teachers. Additional efforts have been made in the development of a national qualifications framework. Higher education has been further aligned with the principles of the Bologna process, but the tertiary education sector suffers from inefficiencies, poor governance and a lack of funding.

The government continued to implement labour market policies on the basis of the National Employment Promotion Plan. Measures include training and employment subsidies for young people without work experience, the long-term unemployed, older persons and vulnerable groups. A new Law on the Restructuring of Unemployment Benefits was adopted. It leads to higher replacement rates in the first three months followed by a gradual decrease thereafter, and offers financial incentives for the unemployed to participate in educational measures. Wage subsidies

were introduced in the context of the introduction of a 32 hour working week. Structural problems persisted as the rate of youth and long-term unemployment remained high at 22% and 5.3%, respectively. Moreover, a slowing economy has led to a drop in employment and participation rates. From an already low level, they dropped slightly to 56.5% and 62.6%, respectively, in the first quarter. *Overall*, low employment rates and structural mismatches between labour supply and demand remain important challenges.

Further progress has been made in developing a knowledge-based economy. The ICT infrastructure is rather well developed, with high internet and broadband penetration rates. The share of the business sector in total spending on research and development has increased. Investment continued to be relatively robust in 2008, mainly due to construction activities, keeping the investment ratio at around 28% of GDP. Private investment accounted for the bulk of it (22% of GDP). However, private investments in the processing and manufacturing industry have remained low, constraining prospects for faster technological change, a more diversified production structure and higher export potential. Public investment remained also relatively strong. In particular, investments in new highways resulted in a further expansion of the network. FDI continued to play a significant role. The total stock of FDI reached € 21.4 billion (44% of GDP). The largest share of cumulative FDI inflows is accounted for by the financial sector (38%), followed by manufacturing (23%) and wholesale and retail trade (15%). However, there has still been little greenfield investment. *Overall*, investment continued to be concentrated in transport infrastructure and the services sector.

Sectoral and enterprise structure

The government decided to restructure the loss-making shipyards through a process of privatisation and started the necessary preparations. This is a key Accession Partnership priority. An agreement was reached with the Commission on the arrangements for the privatisation, enabling international tenders to be launched for the six yards in difficulty. The implementation of the National Restructuring Programme (NRP) for the steel sector has been disrupted by the global economic crisis. Therefore, the NRP as well as individual business plans will have to be revised. The restructuring of the large loss-making railway carrier and the privatisation of subsidiaries has made very limited progress. The objectives of the business plan for 2008 were not fully met, despite some correction of earlier wage increases. The envisaged reduction of the working ratio in 2008 did not materialise and the railway sector continued to receive high levels of budget support. *Overall*, good progress has been made in particular as regards the tendering of the yards with a view to their restructuring through privatisation. However, sustained efforts are required to complete the restructuring of the steel and railway sectors to ensure their long-term viability and competitiveness.

Liberalisation of the telecommunication industry continued. The Croatian Telecommunications Agency continued with activities aimed to stimulate market competition by improving market access to new service providers. This led to further price reductions and to a larger choice of tariff packages for customers. Fixed line competitors raised their market share further from 19% to a still modest 24%. Liberalisation of the energy sector continued gradually and network rules for the transport and distribution of gas have been enacted. However, gas and electricity markets remain dominated by single suppliers, undermining effective competition. The restructuring of the large electricity company has not advanced. *Overall*, despite further legal and regulatory adjustments, competition in network industries remains constrained by dominant incumbent suppliers.

The already large service sector maintained its share in total output at around 65% in 2008. The share of construction increased, from 7.7% to 8.3% of total output, as a result of buoyant activity, while the share of industry declined. The share of the industrial sector and of construction in total employment remained unchanged at around 19% and 9% respectively. Agriculture's share of

employment increased from 12.8% to 13.2%, and that of the services sector dropped accordingly. The already large service sector accounts for two thirds of the economy and the share of construction in total output increased.

In 2008, the SME sector represented around 40% of the corporate sector's total assets, 66.2% of total employment and 65% of total investment. SMEs generated 44% of GDP and more than 40% of total exports. Those indicators remained virtually unchanged compared to the previous year. In order to support the small and medium-sized enterprise (SME) sector the government adopted a new operational plan for 2009. The State Development Bank (HBOR) has been financially strengthened, also through EIB loans, to increase lending to the SME sector on favourable terms. On the other hand, the sector continued to suffer from a cumbersome regulatory framework and inefficiencies in public administration. Access to longer-term financing remained difficult, particularly for newly established businesses. Commercial lending to the SME sector is further restricted by the presence of several subsidised government programmes. *Overall*, while the SME sector continued to benefit from large-scale government support, its share in the overall economy has not increased.

State influence on competitiveness

The government adopted a set of ten anti-recession measures, including reduction of the cost burden, financial strengthening of the State Development Bank (HBOR), and support for tourism, SMEs and the real estate market. The implementation of the anti-crisis programme has been slow and its impact on competitiveness remains uncertain, in particular as regards subsidies for real estate loans, liquidity injections into public companies and import controls. There has been a lack of progress in reducing the large number of levies and fees, mostly at local level, which put a significant financial burden on the business sector. The role of the Competition Agency in monitoring and controlling state aid has been further strengthened, but administrative capacity and enforcement of competition policy needs to be enhanced. The total amount of subsidies in the 2008 and 2009 general government budgets remained high — at around 2.4% of GDP — and a large share has still been provided to loss-making companies. Although horizontal aid has increased relative to sector aid, it still accounts for only a small share of total subsidies. *Overall*, state intervention in the enterprise sector remained substantial and has been further increased by the set of anti-recession measures.

Economic integration with the EU

Croatia is an open economy with total trade in goods and services representing around 92% of GDP. Apart from the export of machinery and transport equipment (mainly ships), tourism continued to be the biggest source of export revenue, representing almost 20% of GDP in 2008. The EU has continued to be the largest trading partner. Its share in total Croatian exports and imports remained at around 61% and 64% respectively. However, in the first six months of 2009, the share of the EU in Croatian imports and exports decreased slightly, as trade with developing countries dropped more slowly than trade with the EU. CEFTA countries represented 10.9% of all Croatian trade in 2008. In the first six month of 2009, the share slightly decreased to 9.9%. In this period, CEFTA countries made 4.8% of total imports into Croatia and 20.1% of all Croatian exports. Around 93% of FDI inflows originate from EU Member States. *Overall*, integration with the EU in the areas of trade and investment remained high.

The average growth in real wages decelerated significantly to 1% in 2008, due to an increase in average inflation. However, wages have increased more strongly than estimated average labour productivity, with the result that unit labour costs have slightly gone up. Indicators of export price

competitiveness have slightly improved as the kuna weakened somewhat vis-à-vis the euro and the US dollar. In the nine months to June 2009, the exchange rate of the kuna depreciated by 3.2% against a basket of currencies in nominal terms. In real effective terms, corrected for consumer price developments, the kuna weakened by a lower rate of 0.6%, as a result of relatively higher inflation in Croatia. *Overall*, standard indicators do not point to significant changes in export price competitiveness.

4. ABILITY TO ASSUME THE OBLIGATIONS OF MEMBERSHIP

This section examines Croatia's ability to assume the obligations of membership – that is, the *acquis* as expressed in the Treaties, the secondary legislation and the policies of the Union. It also analyses Croatia's administrative capacity to implement the *acquis*. The analysis is structured in accordance with the list of 33 *acquis* chapters. In each sector, the Commission's assessment covers progress achieved during the reporting period, and summarises the country's overall level of preparations.

4.1. Chapter 1: Free movement of goods

Progress can be reported regarding alignment on **general principles**. Croatia has continued implementing its Action Plan for compliance with Articles 28 to 30, by amending or annulling legal acts containing restrictions to free movement of goods and by introducing the mutual recognition clause.

In the area of **horizontal measures**, good progress can be reported. Croatia has continued implementing its Strategy for the implementation of the *acquis communautaire* in the field of free movement of goods, which was adopted in November 2007. Approximation in the field of technical requirements has continued with the adoption of the new Act on technical requirements for products and on conformity assessment, which aims to further align the Croatian legal framework with the new horizontal EU *acquis*.

As regards *standardisation*, good progress can be reported. By the end of June 2009 the Croatian Standards Institute (HZN) had transposed 21,368 European standards (ENs). The HZN is an affiliate member of the European Committee for Standardisation (CEN) and of the European Committee for Electrotechnical Standardisation (CENELEC) and applied for full membership of both in June 2009. New internal rules have been set up at the HZN, creating a fast track procedure for adopting European standards in fields that are not covered by HZN mirror committees and providing for regular public enquiries on various groups of harmonised ENs. The reorganisation of the existing technical committees has been completed. As of April 2009, 164 committees were active, covering 65% of the scope of international and European technical committees.

Concerning *conformity assessment*, no progress can be reported.

In the area of *accreditation*, good progress can be reported. The Law on Accreditation and the Statute of the Croatian Accreditation Agency (HAA) have been amended to take into account the new horizontal *acquis* of 2008. The HAA has been promoting accreditation among government institutions responsible for harmonisation of legislation under the new and old approach *acquis*. The HAA signed Cooperation Agreements with the Ministry of the Sea, Transport and Infrastructure and with the Ministry of the Interior in 2009. By July 2009, the HAA had accredited a total of 145 conformity assessment bodies. The HAA increased its staff to 24 permanent employees, 63 lead

assessors (HAA employees and external associates), 98 technical assessors (mostly external associates) and 148 experts (external associates) in eight different accreditation schemes. European cooperation for Accreditation (EA) has continued the evaluation process for granting the status of signatory of its multilateral agreement to the HAA. Preparations in this area are well advanced.

As regards *metrology*, the Law ratifying the Metre Convention was adopted by Parliament in December 2008. Even though the National Metrology Institute (NMI) has been established legally since June 2008, the setting-up of its infrastructure has been delayed in comparison with the Action Plan. Two laboratories in the field of chemistry have been designated as conformity assessment bodies. A National Laboratory for Humidity and a National Laboratory for Ionising Radiation have also been designated. The Laboratories of the State Office for Metrology have been equipped with instruments for testing precious metals, for measurement comparisons within EURAMET and for testing flow meters for liquids other than water. Alignment with the *acquis* in the area of metrology is advanced. The preparations for transferring responsibility for scientific metrology to the NMI are essential to move the chain of traceability at national level through accredited testing laboratories to industry, in time for accession.

Regarding *market surveillance*, there has been significant progress with regard to the State Inspectorate's administrative capacity and enforcement measures. A new State Inspectorate Law on the organisation and role of the State Inspectorate was adopted by the Parliament, abolishing pre-market approval requirements and conferring necessary powers on the market surveillance inspectors. A new Regulation on the System for Rapid Exchange of Information on products presenting risks for consumer health and safety was adopted, stipulating the nature and the operation of the Rapid alert system for measures relating to products posing a serious risk to the health and safety of consumers, and establishing the RAPEX contact point at the State Inspectorate. Further measures are still needed to fulfil all the market surveillance requirements of the EC Regulation 765/2008. Coordination and cooperation between the different market surveillance authorities have been set up in July 2009 with the establishment of the Commission for Coordination and Communication.

In terms of administrative capacity in the Ministry of the Economy, Labour and Entrepreneurship (MELE) some progress can be reported in the Department for Internal Market Coordination, with the recruitment of two additional staff members.

Overall, as regards horizontal measures, basic structures for harmonisation with EU legislation are in place. Further, adequate capacity-building measures are required to enable Croatian institutions to become full members of the relevant European organisations.

There has been some progress in relation to the **old approach** *acquis*, with the adoption of regulations in the fields of medicinal products, veterinary medicinal products, cosmetic products, pre-packaging, aerosol dispensers, motor vehicles, emissions of gaseous and particulate pollutants from engines installed in non-road mobile machinery, textiles, footwear, chemicals, drug precursors, and detergents. A National Strategy for Chemical Safety was adopted in November 2008. Alignment with the *acquis* in the area of the old approach is advanced but further efforts are needed to reach full legislative alignment and to ensure the necessary administrative capacity, with particular regard to pharmaceuticals and cosmetics.

Alignment with the **new approach** *acquis* has been advancing, with the adoption of regulations in the areas of low voltage equipment, machinery, lifts, recreational craft, radio equipment and

telecommunications terminal equipment, electromagnetic compatibility, cableway installations, pressure equipment and simple pressure vessels, noise emissions by equipment for use outdoors, pyrotechnic articles, construction products and medical devices. Alignment with the *acquis* in the area of the new and global approach is well on track, but further efforts are still needed, with particular regard to equipment and protective systems intended for use in potentially explosive atmospheres, safety of toys, and eco-design requirements for energy-using products.

Concerning **procedural measures**, some progress can be reported. A new Regulation on notification procedures in the field of standards, technical regulations and regulations on information society services was adopted in 2009, thus transposing Directive 98/34/EC as amended by Directive 98/84/EC. Alignment in the field of procedural measures is advanced, but further efforts are still needed to fully transpose Directive 91/477/EEC as amended by Directive 2008/51/EC.

Conclusion

Good progress has been made in the field of the free movement of goods. Alignment with the *acquis* in this chapter has further progressed and is well advanced, but some elements are not yet fully in place, notably with regard to conformity assessment, metrology and market surveillance. Croatia needs to continue efforts to fully align with the *acquis* and to build the necessary capacity to ensure its effective implementation and enforcement upon accession.

4.2. Chapter 2: Freedom of movement for workers

Croatia already largely fulfils the *acquis* requirements in the area of **access to the labour market**.

Good progress can be reported on future participation in the **EURES** (European Employment Services) network. The organisational structure of the Croatian Employment Service (CES) is being adjusted and administrative capacity strengthened as regards services related to mobility and free movement of labour. This is a key element for the accession negotiations in this chapter. Language skills of potential EURES advisers are being improved and the CES has become acquainted with the requirements related to connection to the EURES Job Mobility Portal upon accession to ensure that all job vacancies handled by the public employment services are displayed on its public website and can therefore be made available for publication on the Portal. Various training activities in relation to EURES have been carried out, among others in the regional employment offices. In this area, Croatia is well on track.

There has been good progress on **coordination of social security systems**. Sufficient administrative capacity is being developed to apply the *acquis* in this field. This is a key element for the accession negotiations in this chapter. A wide range of professional training in all branches of social security as well as language courses have been offered for the State administration bodies. Preparations in this area are well on track.

Preparations are ongoing for the introduction of the **European Health Insurance Card** as from accession.

Conclusion

Good progress has been made on this chapter. A satisfactory level of legal alignment has been reached. However, sustained efforts are needed to develop the necessary administrative capacity,

notably for carrying out a potentially wider range of tasks in the area of coordination of social security systems.

4.3. Chapter 3: Right of establishment and freedom to provide services

Progress can be reported on the **right of establishment**, although further work is needed to ensure full alignment with the *acquis*. The Act amending the Aliens Act eliminated the requirement of a business or work permit for EU and EEA citizens, as from the date of accession. The amended law on the temporary residence tax introduced equal treatment of Croatian and EU citizens with regard to the payment of the tax on secondary residences. The amendments to the Healthcare Act, the Act on Humanitarian Landmine Clearance, the Act on Performing the Activities of Design, Building Surveillance and Construction and the Act on Geodetic Activity waive Croatian citizenship and excessive language knowledge requirements as of the day of Croatia's accession. The Act on Libraries and the Act on Archives and Archival Institutions provide for free establishment of such institutions by domestic and foreign natural and legal persons, as of Croatia's accession to the EU. However, a number of restrictions on the right of establishment continue to exist in several sectors, in the form of authorisation regimes and the one-office-rule.

Some progress has been made regarding the **freedom to provide cross-border services**. The new Law on Private Detectives enabled certified detectives from the EU Member States to provide their services in Croatia upon its accession to the EU. A working group has been established to work on the alignment with the Services Directive. However, several provisions in the national legislation are still not in line with Article 43 of the EC Treaty and the preparations for the implementation of the Services Directive are at an early stage. Administrative capacity in the area of coordination and alignment with the *acquis* as regards freedom to provide services requires further efforts.

Further progress has been made in the field of postal services, where legislative alignment with the *acquis* is well advanced. The Postal Services Act was adopted in July. Amendments to the primary legislation already envisage implementation of most of the regulatory elements of the 3rd Postal Directive and lay down a detailed timetable for gradual market opening (full market opening envisaged for 31 December 2012) and confer extensive regulatory and supervisory powers on the National Regulatory Authority for the postal sector. However, full alignment with the postal *acquis* (mainly provisions of the 3rd Postal Directive) has not yet been achieved. Implementing legislation laying down conditions for the provision of postal services and rules on the postal system of the public operator was amended.

The capacities of the Council of the Croatian Post and Electronic Communications Agency (HAKOM) have been strengthened, as three new members were appointed. The addition of two further resources to the **Postal Services** Department of HAKOM has brought the administrative capacity of the office to a satisfactory level. At the same time the Croatian Post, the designated universal service provider, adopted a strategic framework to prepare for future full market opening.

Some progress has been made on the **mutual recognition of professional qualifications**. However, the minimum training requirements for the medical professions (doctors, dentists, midwives, nurses, pharmacists) are still not in line with the *acquis*. As regards dentists, the professional and academic title ('stomatology') used is not recognised under the *acquis*. The new Act on Regulated Professions and the Recognition of Foreign Professional Qualifications regulates both the recognition of foreign professional qualifications and creates a legal basis to ensure that the minimum training requirements of the *acquis* will become applicable as from the day of accession. Administrative capacity to deal with the mutual recognition of qualifications needs to be strengthened. Preparations in the field of mutual recognition of professional qualifications are advancing.

Conclusion

Progress has been made in this chapter, in particular on the mutual recognition of professional qualifications and postal services, and overall alignment with the *acquis* is at a reasonable level. Further work is required in order to complete alignment. The remaining obstacles to the right of establishment and freedom to provide services need to be removed and further efforts are needed in the area of mutual recognition of professional qualifications. Administrative capacity needs to be reinforced.

4.4. Chapter 4: Free movement of capital

Some progress can be reported concerning the **free movement of capital**. As regards real estate, the Act on Ownership and other Real Rights was amended and entered into force in February 2009. According to this Act and in line with the obligations under the SAA, EU nationals are now entitled to acquire ownership rights over real estate under the same conditions as Croatian nationals. Moreover, procedures which had been initiated by citizens of EU Member States for acquiring property ownership in Croatia but were not finalised before 1 February 2009 have been discontinued *ex officio*. However, restrictions on acquisition of agricultural land and nature-protected land remain in place.

As regards other capital movements, amendments to the Deposit Insurance Act eliminated as of January 2009 privileged access of the public sector to financial institutions. However, a number of restrictions remain. Due to the global financial situation, Croatia decided to postpone the liberalisation of certain remaining capital movements. The liberalisation of short-term financial loans to non-residents has been postponed until February 2010. The liberalisation of transfers abroad, relating to gifts and grants, transactions with derivatives, the use of loans from abroad through accounts abroad, payments and collection in foreign cash, taking cash into and out of the country, transfer into or out of the country of materialised securities and transactions in foreign exchange markets abroad, was postponed until January 2010. Some discriminatory provisions still remain in Croatian legislation, in particular concerning the use of assets in building societies. The special rights or ‘golden shares’ that the government has retained in certain privatised companies will need to be abolished by the day of Croatia’s accession to the EU.

With regard to **payment systems**, no progress can be reported.

As regards **anti-money laundering** (AML), a new AML law providing for improved alignment with the *acquis* entered into force in January 2009. Relevant implementing legislation has been adopted. There has been a gradual reduction in the number of suspicious transactions reported to the Croatian Financial Intelligence Unit (FIU). This followed changes in the reporting system aimed at providing the FIU with notifications of a higher quality. The Criminal Code has been amended in order to widen the definition of the money laundering offence and to bring it into line with the requirements of both the Vienna and the Palermo Conventions. The confiscation regime has been extended to all property related to a perpetrator of organised crime or corruption offences; the possibility of reversal of the burden of proof has been introduced. The scope of the terrorist financing offence has been extended and public incitation to terrorism, recruitment and training for terrorism can also now be prosecuted. The FIU has been further strengthened through an increased number of staff.

Monitoring and supervision of reporting entities remains inadequate, however, especially outside the banking sector, and the enforcement record (including convictions, confiscations, seizures and asset freezing) is still weak. The notification system itself has led to only limited prosecutions

and/or conviction. Implementation continues to be affected by poor functioning of the judiciary. There remains a backlog of cases concerning AML offences in courts. Moreover, inter-agency cooperation, albeit improved, still leaves considerable room for improvement.

Conclusion

There has been some progress in this chapter, mainly as regards liberalisation of the real estate market and legislative changes in the anti-money laundering area. Overall, a reasonable level of alignment has been achieved. Further efforts will be needed, especially with implementation and enforcement of AML legislation, including inter-agency cooperation, and with completing liberalisation of capital movements and alignment with the payment services *acquis*.

4.5. Chapter 5: Public procurement

Good progress can be reported as regards **general principles**. The amendments to the Public Procurement Law and relevant implementing legislation were adopted, aligning to a large extent the Croatian legal framework with the *acquis*. The new Concessions Law and the Public-Private Partnerships (PPPs) Law entered into force in January 2009. The Strategic Framework for the Development of Public-Private Partnerships (PPPs) was adopted and relevant manuals in the area of PPPs were issued. The Concessions Register was established within the Ministry of Finance and is fully operational. In line with the ‘Roadmap for harmonisation of special regulations governing concessions with the Concessions Law’, several pieces of sectoral legislation have been amended.

With regard to *administrative capacity*, the Department for the Public Procurement System (DPPS) successfully ensured that a coherent public procurement policy was adopted at the institutional and legislative level. The work of the DPPS is positively perceived by both economic operators and contracting authorities. Cooperation between State bodies engaged in public procurement issues has significantly improved. An Implementation Monitoring Committee was established to oversee progress as regards the Strategy for the Development of the Public Procurement System. The capacities of the Ministry of Finance were strengthened by two extra employees dealing with concessions and fiscal aspects of PPPs. A new Agency for Public-Private Partnership was established as a body responsible for evaluation and approval of PPP project proposals, tender documents and final draft contracts pursuant to the provisions of the PPP Law. The agency employs 12 people.

However, the Guide for Concessions, the alignment of the sectoral legislation regulating concessions and the elaboration and implementation of methodological tools for fostering the administration of the new PPP legislation is still to be completed. The Department for the Public Procurement System has yet to enhance its monitoring capacities to prevent irregularities in PP procedures.

Good progress has been made in the area of **award of public contracts**. All contract notices above 70,000 Croatian Kuna are published in the Official Gazette, thus ensuring transparency. Contracting authorities and entities are generally familiar with the procurement procedures. Open procedures are the most commonly used, usually together with the lowest price award criterion. A new rule has been introduced which will require that as of January 2010 at least one member of the selection committee is certified as a public procurement specialist.

Numerous training courses have been provided at central and local level for both economic operators and contracting authorities. The training covered in particular the areas of public contracts, concessions and PPPs, legal protection and the issue of ethics and conflicts of interest. However, within contracting authorities, the overall level of sensitivity as regards potential conflicts

of interest and integrity is low. Further training activities are required for contracting authorities/entities on conflicts of interest, and to get them used to applying award criteria other than the lowest price.

Some progress can be reported in the **remedies system**. The competences of the State Commission were expanded to cover remedies on concessions and PPPs. The Law on the State Commission for the Supervision of Public Procurement Procedures has yet to be amended. The State Commission takes an active part in training contracting authorities and bidders in the field of legal protection. Due to changes in legislation widening the scope of possible request for review, the total number of complaints increased considerably as compared to the previous reporting period. The State Commission has increased its capacity to deal with them and its decisions are issued on average within 38 days. However, its administrative capacity — especially in view of an expected further increase in the number of cases — is not sufficient. Judicial review of State Commission decisions by the Administrative Courts takes on average several years, which is problematic in terms of an effective remedies system.

Administrative capacity and coordination mechanisms of the main stakeholders in the public procurement system still need further strengthening, in particular as regards anti-corruption activities and integrity. The scope for corruption remains wide. The capacity of the procuring entities to apply the public procurement legislation correctly, efficiently and transparently needs to be enhanced in order to reduce the potential for irregularities, including fraud and corruption in public procurement procedures. Significantly improved scrutiny of actual execution of contracts is essential.

Conclusion

Good progress can be reported under this chapter in particular as regards completion of the necessary institutional set-up. Overall, preparations are at an advanced stage. However, legislative alignment still needs to be completed. Practical guides for implementing the legislation need to be further developed. Administrative capacity needs to be further enhanced at all levels of the procurement system, in particular with a view to effectively fighting corruption and tackling irregularities.

4.6. Chapter 6: Company law

Progress has been recorded in the field of **company law**, where the legislation is largely aligned with the *acquis* and work is ongoing with a view to complete the alignment.

New instructions were issued on methods and conditions of electronic communication with the Court Register competent for registration of limited liability companies. A pilot project on electronic communication with the Court Register for limited liability companies was extended. Online registration is now possible in 10 commercial courts, but not yet in Zagreb. Code systems of the Court Registers and instructions on their keeping remain to be further regulated.

Relevant departments within the Ministry of Justice are understaffed.

There has been some progress in the field of **corporate accounting**. The legislation is to a large extent aligned with the *acquis*. Several pieces of implementing legislation were adopted, including on the structure and content of the annual financial accounts of investment companies.

A Handbook on the Implementation of Croatian Financial Reporting Standards (CFRS) was published. The CFRS Committee continued translating and publishing international accounting standards and related interpretations issued by the International Accounting Standards Board.

The Register of Annual Accounts is accessible via the internet and maintained by the Financial Agency FINA. FINA received 79,065 annual accounts, 36,918 of which were published.

There has been good progress in the field of **auditing**. The amendments to the Audit Act aligning the legislation with the 8th Company Law Directive were adopted and entered into force. These set up an external quality assurance system and public oversight processes for the auditing profession. The Audit Public Oversight Committee started operating but is not yet fully functional. The Croatian Chamber of Auditors hired one additional expert, but further strengthening is needed to ensure proper quality assurance checks. The Ministry of Finance has established a Department for Financial Reporting for issues of public policy in auditing and accounting, but overall resources remain to be allocated. Only two employees are currently working in the Department.

Conclusion

Overall, some progress can be reported in this chapter. Alignment with the *acquis* is on track. More remains to be done in the area of auditing as regards the implementation of the new legal provisions and the strengthening of administrative capacity.

4.7. Chapter 7: Intellectual property law

There has been little progress in the field of **copyright and neighbouring rights**, where Croatian legislation is largely in line with the *acquis*. The new Criminal Procedure Act aligned Croatian legislation with the Convention on cyber crime as regards copyright and related rights. Following the publication of the Tourism Action Plan, which recommended a reduction of copyright fees for authors, performers and phonogram producers during the tourism season, the copyright holders' association agreed a 10% reduction of the fees in favour of the hotel operators' association. Such intervention of the national authorities, albeit in the form of a recommendation, may be contrary to the exclusive rights of authors and to the right to equitable remuneration of performing artists and phonogram producers.

Some progress can be reported in the area of **industrial property rights**, where Croatian legislation is already highly aligned with the *acquis*. The outstanding minor changes to bring the legislation fully into line with the *acquis* in the field of patents, trade marks, industrial design and topographies were adopted. The provisions on the cut-off date for Supplementary Protection Certificates (SPCs) and exhaustion of patent rights in the field of biotechnology were also amended and aligned with the *acquis*. The Croatian Chamber of Registered Patent and Trademark Representatives was formally established in July.

Some, but uneven, progress can be reported in the field of **enforcement**. Efforts to protect right holders and consumers have been put in place in most enforcement bodies, in particular at the Customs Administration. A new regulation was adopted to fully harmonise the procedure for the renewal of the protection of rights by Customs with the EU *acquis* and to strengthen inter-agency cooperation. Intellectual property crime is of growing concern for the health and safety of consumers and on account of the increasing involvement of organised crime groups. Management and training efforts need to be stepped up and inter-agency cooperation has to be further enhanced. Further efforts are needed to strengthen the capacity of police and prosecutors in the field of protection of intellectual property rights, including by allowing the use of enhanced investigation powers, such as technical surveillance, to detect IP crimes.

As regards administrative capacity, the State Intellectual Property Office (SIPO) has been further strengthened with 25 new staff and a self-financing model has been introduced. The Board of Appeal, providing the right to appeal against first instance decisions of SIPO, started operations from 1 June 2008 and issued decisions at a satisfactory rate. Out of 72 appeals received during its first 9 months of operations (June 2008 to March 2009), 48 were adjudicated.

Conclusion

Progress can be reported as regards both legislative alignment and enforcement. Alignment with the *acquis* has reached a very high level. Further efforts are required to strengthen the overall awareness of intellectual property rights in society at large, including with regard to the dangers for health and safety. Attention should be given to the increasing involvement of organised crime groups in intellectual property rights-related offences.

4.8. Chapter 8: Competition Policy

Significant progress can be reported in the field of **antitrust, including mergers**. The Croatian Competition Agency (CCA) has hired new staff but more remains to be done to further strengthen the Agency's administrative capacity. A new Competition Act was adopted, in line with the *acquis*. The Act empowers the Agency to impose fines and to conduct a leniency programme, thereby strengthening the Agency's deterrent effect and enforcement policy, in particular against cartels. With regard to the protection of the rights of defence, the Act introduces the obligation for the Agency to submit statements of objection to the parties. It also makes CCA decisions subject to review by the High Administrative Court of Croatia.

The CCA took 41 decisions in antitrust and merger including 19 merger cases, 3 on restrictive agreements, 3 on cases of abuse of a dominant position and 16 advocacy cases. However, the CCA did not take any decision against hardcore cartels.

In the field of transport, one airport was found to have abused its dominant position as service provider. In the field of energy, the CCA concluded that a firm had abused its dominant position in the market of gas supply. On its own initiative, the CCA concluded that one of the leading companies in telecom services had used prohibited agreements to set the minimum reselling prices. The CCA has continued to provide the government with assessments of draft laws as well as other expert opinions. Preparations in the field of antitrust, including mergers, are well on track.

There has also been some progress in the field of **state aid**. The CCA issued 36 opinions and decisions. In one of its opinions, the CCA concluded that the Croatian Broadcasting Act, which governs the financing of Croatian National Television, was not in line with the SAA State aid rules and the Croatian State Aid Act. This is a key element in the accession negotiations in this chapter. The CCA has stepped up its efforts to improve the notification rate by aid grantors in national, regional and local governments. But more remains to be done on competition advocacy, particularly at the regional and local levels.

The restructuring of the steel and shipyard sectors in Croatia are key elements in the accession negotiations in this chapter. With regard to the shipbuilding sector, Croatia has made substantial progress. The launch of international privatisation tenders for the six yards in difficulty marked the beginning of a restructuring process through privatisation. The tender documentation is in line with the requirements of the SAA State aid rules and the *acquis*. Croatia's steel industry faced difficulties due to the global economic and financial crisis. Production in Željezara Split was brought to a halt in mid-April. At the steel mill of CMC Sisak, a deviation from the original plan occurred while at the same time new investments were launched. The National Restructuring Plan and Individual

Business Plans adopted by the government in June 2008 have become obsolete and will need to be revised.

Conclusion

Significant progress has been achieved on this chapter in particular as regards adoption of the Competition Act and the tendering of the shipyards in difficulty with a view to their restructuring through privatisation. Overall, a reasonable level of alignment has been achieved. However, sustained efforts are required in order to complete the restructuring of the shipyards. Furthermore, work remains to improve the CCA's enforcement record against cartels, to align the Croatian Broadcasting Act, and in the steel sector.

4.9. Chapter 9: Financial Services

There has been good progress in the field of **banks and financial conglomerates**. Croatia adopted legislation implementing the Credit Institutions Act, thus further aligning Croatian banking legislation with the *acquis*, in particular the Capital Requirements Directive (CRD), which is currently under review at EU level. Implementation of the Credit Institutions Act provisions relating to capital adequacy was postponed until 31 March 2010. The Law on Financial Conglomerates was adopted, providing for the additional supervision of regulated entities, which have been authorised to operate based on laws regulating activities of credit institutions, investment companies, insurance and reinsurance companies and companies forming a financial conglomerate. The law is already in force except for the provisions regulating activities and supervision of financial conglomerates that have their registered office in the EU, which will enter into force upon Croatia's accession to the EU. The framework for risk-based supervision was adopted, and a new working group for implementation of the CRD was set up. Home-host supervisory coordination has improved. Work still needs to be done on cross-sector cooperation and cross-border coordination for crisis preparedness and management. The process of transforming savings and loan cooperatives into credit unions or savings banks was completed at the end of 2008. As a response to the global financial crisis, the Croatian National Bank performed a quantitative impact assessment on banks' capital adequacy in line with the recommendations of the Financial Stability Forum. Moreover, the Deposit Insurance Act was amended and the level of guaranteed bank deposits was substantially increased.

Some progress can be reported with regard to winding-up procedures. More details on offences and penalties related to the winding-up of credit unions and on supervision of saving and loan cooperatives in a process of winding-up were included in the Law on Credit Unions. The Ministry of Finance has issued implementing legislation regulating the inspection and supervision of the winding-up of savings and loan cooperatives.

The Croatian Financial Services Supervisory Agency (HANFA) and the Croatian National Bank (HNB) adopted the ordinances establishing the layout and the content of annual accounts for entities under their supervision. The Croatian National Bank has signed Memoranda of Understanding with the French Banking Commission and the German Supervisory Agency, regulating cooperation in banking supervision.

Further progress can be reported in the field of **insurance**, where a good level of alignment has already been reached. Legislation in the area of compulsory motor insurance has been further improved. By amending the Insurance Act and adopting the related implementing legislation, Croatia has aligned its legislation in the outstanding areas of non-life insurances, insurance mediation and supervision of reinsurance companies. Croatia has also aligned its legislation with

the EU *acquis* in the area of investment restrictions concerning technical reserve coverage of insurance undertakings and calculation of the solvency margins in the Life and Non-Life Insurance Directives. Provisions of the *acquis* concerning certain investment rules were also transposed and will become applicable upon Croatia's accession to the EU. Alignment with the Directive on supervision of insurance groups was also completed with the adoption of amendments to the Insurance Act as well as relevant implementing legislation in the Ordinance on supplementary supervision of insurance groups. Further efforts are still required to reach full alignment with the pension insurance *acquis* and life and non-life insurance legislation, as well as to guarantee the proper functioning of the insurance and occupational pensions markets.

There has been some progress concerning the **financial market infrastructure**. Croatia adopted regulations implementing the Law on Settlement Finality in payment systems and in systems for settlement of financial instruments.

Progress can be reported in the area of **securities markets and investment services**, where a good level of alignment has been already reached. Croatia adopted the legislative framework regulating special criminal offences against the capital market. HANFA has also adopted implementing legislation stemming from the Capital Market Act. Amendments to the Capital Market Act to fully align with the MAD and Prospectus Directive were adopted in July. Alignment with the collective investments *acquis* — UCITS Directive (2007/16/EC) — has also been achieved. HANFA, all four mandatory pension funds and the four largest companies managing open-ended investment funds have jointly established the Fund for Protection of Investors.

As regards *administrative capacity*, the Financial System Department in the Ministry of Finance, responsible for drafting financial legislation, employs 21 people. Administrative strengthening through additional training and additional staff would be advisable. The National Bank's Prudential Regulation and Bank Supervision Department hired 8 additional staff. HANFA has continued to strengthen its administrative capacity, by employing 2 new staff (reaching 124 in total) and by providing training programmes on risk-based supervision. HANFA was also active in educating the broader public and investors, as well as professionals, police, state attorneys and journalists. Croatia should continue its efforts to strengthen HANFA's administrative capacity and to improve its arrangements for consultation with the private sector.

Conclusion

Significant progress can be reported on this chapter, both as regards alignment of legislation and strengthening of administrative capacity. Legislative alignment is very advanced, but further efforts are needed regarding implementation. Efforts need to continue to strengthen the supervisory authorities' capacity to perform their supervision function and improve consultative interaction with the financial sector.

4.10. Chapter 10: Information society and media

Good progress has been made in the field of **electronic communications and information technologies**. Following the adoption of the Electronic Communications Act, the necessary implementing legislation has been adopted. Liberalisation of the sector has continued to progress significantly, in particular in the broadband market. As of January 2009, the fixed broadband penetration rate was 11.80%, mainly through xDSL technology, with the incumbent holding 89% of the market. Mobile penetration has reached around 130%. There is a significant number of UMTS subscribers, but few active users of mobile internet (around 6% of fixed broadband users). Legislative and policy improvements have taken place with the aim of facilitating the building of

mobile infrastructure. However, further efforts are needed to achieve concrete results. Market analysis procedures and regulations are well under way, but one critical aspect relates to costing methodology to be applied to dominant operators. A recent governmental initiative has been to introduce a 'crisis tax' on mobile services: this measure goes against the current EU strategy to promote Europe's digital economy as one response to the present economic downturn.

Administrative capacity has been strengthened in the Directorate for Electronic Communications and the Postal Service within the Ministry of the Sea, Transport and Infrastructure. The level of competence at the Croatian Post and Electronic Communications Agency has been further enhanced. A new director has been appointed after an open recruitment procedure. Measures have been taken to increase the level of transparency of the work of the regulator and improve the accessibility of the relevant information to the public. The Telecommunications Users Council has been replaced by the Consumer Protection Unit of the regulator as its advisory body. Representatives of consumer protection associations have been appointed to this advisory body. Preparations in this area are well advanced.

Some progress has been made in the area of **information society services** and electronic commerce. Further amendments to the Electronic Commerce Act have been adopted aimed at completing legal alignment in this field. An e-Government Strategy for the period 2009–2012 has been adopted. Preparations in this area are reaching completion.

Some progress can be reported in the field of **audiovisual policy**. Preparations for the introduction of digital television are under way. The Croatian Audiovisual Centre has been established, and it has joined European Film Promotion. However, some interference in the media landscape by mainly economic and partly political interest groups has continued. Also, anticompetitive State aid to the national broadcaster has continued. Nevertheless, preparations in this area are well advanced.

Conclusion

Good progress has been made in this chapter. A good level of legal alignment has been reached. Efforts need to continue to strengthen the capacity of the two national regulators to implement correctly the legal framework, including on mobile infrastructure development. Efforts from all levels of government are necessary to sustain liberalisation of all segments of electronic communications, and to ensure a level playing field in the audiovisual markets. The recent tax measures on mobile services are rather counterproductive in that respect.

4.11. Chapter 11: Agriculture

Progress was achieved as regards **horizontal issues**. Croatia adopted the Act on State Support for Agriculture and Rural Development as a first step in reforming the sector. However, substantial effort is still needed to fully align the agricultural support system with the Common Agricultural Policy (CAP). As regards the Paying Agency (PA), Croatia adopted the Act on the establishment of the Paying Agency (PA) and appointed the Agency's managing board. Substantial efforts are needed to make the PA operational, as well as the Integrated Administration and Control System (IACS)/Land Parcel Identification System (LPIS), which are key elements in the accession negotiations in this chapter. Sufficient and timely staffing of the PA as well as the allocation of budgetary resources are of crucial importance. Efforts are needed to implement the LPIS at national level. A good level of *acquis* alignment has been achieved for the collection and processing of agricultural data. Progress can be reported on the implementation of the Farm Accountancy Data Network (FADN) with a requirement to further secure necessary human and budgetary resources.

As regards **common market organisation (CMO)**, progress is ongoing as a result of several activities regarding different sectors and horizontal aspects of the single CMO. Continued efforts are essential to implement the CMO, which is a key element of the accession negotiation in this chapter. Legislation on wine as well as the vineyard register needs to be adjusted to the new implementing regulation. A new Ordinance on spirit drinks has been adopted; its alignment with the *acquis* remains to be confirmed.

In the field of **rural development**, Croatia is in the process of completing the SAPARD programme. Preparations are well advanced for the implementation of certain rural development measures under the Instrument for Pre-Accession (IPARD). Further strengthening of the administrative structures and capacity is needed to correctly and successfully implement rural development programmes. Timely implementation of the IPARD programme remains a crucial factor for its success.

Croatia continued alignment with EU legislation in the areas of **quality policy** and **organic farming**.

Conclusion

Progress can be reported in this chapter, in particular regarding the collection and processing of agricultural data, the common market organisation and rural development. Alignment continued in the field of quality policy and organic farming. Overall, preparations are moderately advanced. Croatia needs to adjust legislation and structures regarding the *acquis* for wine. Substantial efforts are still required to establish the paying agency and the Integrated Administration and Control System as well as the Land Parcel Identification System. Preparations need to be accelerated and plans prepared on the basis of realistic expectations. Further alignment of the support schemes with the CAP is essential to prepare for a smooth transition to the CAP. In rural development, the absorption capacity for EU pre-accession funds needs to be improved.

4.12. Chapter 12: Food safety, veterinary and phytosanitary policy

Good progress can be reported in the implementation of the strategy for transposition, implementation and enforcement of the *acquis* for food Safety, veterinary and phytosanitary policy. Further progress can be noted as regards **general food safety**, where Croatia adopted implementing legislation based on the already aligned Food Act. Continued efforts are required to finalise transposition and ensure implementation of the new legislation as well as the necessary administrative and control capacity.

Good progress has continued in the veterinary field with the adoption of several implementing regulations based on the Veterinary Act, which is in accordance with EU requirements. A compliant system for financing of veterinary inspections has been established. The recruitment of additional official veterinaries has started. Preparations for construction and fitting-out of Border Inspection Posts (BIPs) have started. Implementation of the identification of animals and the registration of their movements continues. Croatia continued implementing the action plan for control and eradication of Classical Swine Fever. Additional administrative efforts are needed to secure a fully EU-compliant control system, which is a key element of the accession negotiations.

In the area of **placing on the market of food and feed**, good progress can be reported. The national programme for the upgrading of establishments for food and feed of animal origin, which is a key element of the accession negotiations, is being finalised. A system to control **raw milk** has been put in place. Procedures are in place to control and improve milk quality and to prevent the use of non-

compliant milk. However, efforts remain to be made to increase the reliability of the control system. Increased effort is needed to finalise upgrading plans for all establishments.

In the area of **animal by-products (ABP)**, deficiencies need to be addressed regarding official controls and establishments to ensure that ABP are handled in line with EU legislation.

Croatia has made progress in setting up a system for controls of **animal welfare** standards. Administrative capacity and procedures have improved. Efforts are needed to improve implementation of controls.

Good progress continued in the area of **phytosanitary** issues, with the adoption of implementing legislation in the fields of plant health, plant protection, seeds and planting material as well as the registration of varieties of agricultural plants. Transposition of the EU *acquis* into national legislation is advanced as regards the placing on the market of plant protection products and maximum residue limits of pesticides. Preparations for construction and fitting-out of BIPs have started. Additional training for staff is needed.

Conclusion

Good progress has been made, in particular with the passing of implementing legislation and its implementation. Overall, preparations are advanced. Continued efforts are required to finalise transposition and implementation of the EU *acquis*, in particular regarding implementation of the national programme for the upgrading of establishments for food and feed of animal origin and the securing of the necessary administrative and control capacity.

4.13. Chapter 13: Fisheries

Good progress can be reported in the areas of **resource and fleet management** and **inspection and control**. Croatia started to implement legislation on landing declarations and sales notes. The programme for the fishing vessel register is functional. Installation of the satellite-based vessel monitoring system (VMS) on board the vessels concerned is well advanced. The fisheries monitoring centre (FMC) is established and staffing continues. Equipment and administrative capacity of the fisheries inspection services has improved. As for fish statistics, a high level of *acquis* alignment has been achieved for the collection and processing of fisheries data and statistics on fishing vessels. However, the register of all commercial fishing vessels needs to be finalised and subsistence fishing vessels addressed. An entry-exit scheme is still lacking. Administrative and operational inspection capacity, which is a key element of the accession negotiations, needs further strengthening, in particular concerning the recruitment and training of additional fisheries inspectors to carry out controls at the coast.

Limited progress can be reported on **market policy**. Collection of information on species, quantities and prices has started. While wholesale fish markets have been developed in Rijeka and Poreč, the latter is still not in full use. Increased effort is needed regarding the establishment of producers' organisations and alignment of marketing standards.

There has been some progress on **structural action** and **State aid**. Croatia started designating and strengthening the administrative structures necessary to implement the European Fisheries Fund. Effort is still needed to strengthen the institutional framework and to finalise the national fishery strategy. Croatia needs to align State aid with the *acquis*.

In the area of **international agreements**, Croatia is taking steps to implement the recommendations of the International Commission for the Conservation of Atlantic Tuna (ICCAT) regulating catches,

farming and trading of tuna. However, more progress needs to be made regarding adjustment of the fleet and farming capacity.

Conclusion

Croatia has made good progress in the field of fisheries. Overall, preparations are well advanced. Croatia will need to step up its efforts to close the remaining gaps in the areas of fleet management, inspection and control, structural action and state aid.

4.14. Chapter 14: Transport policy

Good progress can be reported in the field of **road transport**. The National Security Policy for digital tachographs has been adopted by ERCA and the card issuing authority has been set up, which constitute important elements in this chapter. New inspectors are being employed, the necessary equipment for performing checks is being procured and professional qualification courses are ongoing in order to develop adequate administrative capacity to enforce the rules relating to the road transport *acquis*, including roadside checks. However, targeting of checks should be revised in order to increase the control over national hauliers.

There has been some progress in the area of **rail transport**. The law on the railway regulatory body has been amended in order to improve its functioning. The board of the rail regulator has assumed its functions and has taken a number of decisions related to staff measures. The derailment of a passenger train near Split at which several persons were killed in July 2009 resulted in the dismissal of the infrastructure management company's CEO. Croatia reinforced its legal framework in June 2009 to foresee the application of a set of criteria aimed at ensuring the independence of the infrastructure manager from the railway undertakings, despite both being under one holding.

There has been some progress in the area of **inland waterways transport**. The basic legislative framework has been aligned, but the relevant ministerial regulations still remain to be enacted.

Shortcomings related to **combined transport** remain.

Good progress can be reported in the area of **air transport**. The new Aviation Act was adopted in June 2009. An independent Civil Aviation Agency was established and has started to function. Relations between the Croatian Civil Aviation Agency and EASA have been put on a formal footing by a working arrangement signed in July 2009. Nevertheless, an assessment performed in September 2009 by the European Aviation Safety Agency indicates that Phase 1 of the European Common Aviation Agreement, which is one of the key elements in this chapter, is not yet fully implemented, in particular in the area of aviation safety. Progress has been made as regards the Single European Sky legislation although further efforts are needed to ensure its full compliance. Further *acquis* alignment is required in the area of air traffic management as regards the certification and designation of the air navigation service provider, the nomination of a notified body, complete transposition of the air traffic controller directive and of the interoperability implementing rules, and the implementation of the flexible use of airspace regulation. Legislation on ground handling and slot allocation still need to be aligned with the relevant Community rules and there is a need to take the necessary steps to enact the ban on Chapter 2 aircraft.

Some progress can be reported in the area of **maritime transport**. Implementation of the Vessel Traffic Monitoring Information System (VTMIS) is ongoing. The detention rate of Croatian-flagged vessels in the Paris MOU area decreased from 7.7% in 2007 to 4.1% in 2008. A maritime safety verification mission was conducted in March 2009. It identified several important shortcomings that hamper Croatia's ability to implement the EU *acquis*, in particular the role of the Croatian Register

and its relationship with the maritime administration. Croatia needs to strengthen flag and port State capabilities, make progress on VTMIS and ensure proper development of port reception facilities. Legislation on maritime cabotage is not in line with the *acquis*. Further alignment is also required as regards maritime security.

As regards **State aid** in this sector Croatia has not yet fully aligned its legislation.

Croatia intends to take part in the activities of the Galileo **satellite navigation** programme when operational.

Conclusion

There has been some progress in this chapter. Overall, there is a reasonable level of alignment. Croatia needs to continue its efforts to improve administrative capacity in the maritime transport sector, in the Civil Aviation Agency, in particular in view of aviation safety, and in the railway regulatory authority, in particular through training of staff. The new provisions concerning the independence of the rail infrastructure manager have to be further implemented under the supervision of the regulatory body in every day practice. Further legislative alignment is needed not least in the aviation and maritime cabotage sectors.

4.15. Chapter 15: Energy

There has been some progress in the area of **security of supply**. Croatia adopted the rules for usage of the gas storage system. Croatia has taken important steps towards achieving the mandatory 90 days of emergency oil stocks. There are no developments in relation to the establishment of a crisis management body or intervention plans. Under the new Mining Act, which was adopted in June 2009, authorisations for prospecting, exploration and production of hydrocarbons will be granted on the basis of a non-discriminatory principle in line with the *acquis*. In the area of security of supply Croatia partially meets its targets.

Progress in the area of the **internal energy market** has been good. Implementing legislation relating to the organisation of the gas market and network rules for gas transport and distribution have been enacted. The Energy Law and the Electricity Market Law have been amended. New rules on allocation of cross-border capacity for electricity have been adopted and were in force as of January 2009, foreseeing that as of 2010 the yearly allocation of capacity will be in full compliance with the *acquis*. The legal framework in Croatia complies with the *acquis* of the second internal energy market package. However, single suppliers continue to dominate the electricity and gas markets. Croatia will now need to focus on implementing the requirements of the recently adopted third internal energy market package. Preparations in this area are advanced.

The regulator is fully functional and continues to recruit additional staff. However, no progress has been made towards a clear distinction and separation of tasks between the regulator and the Ministry.

Little progress can be reported in the area of **renewable energy sources (RES)**. Amendments have been made to implementing legislation on incentive fees for the production of electricity from renewable sources. The Act on Biofuels for Transport was adopted in May 2009 and aims to fully align Croatian energy legislation with the previous Biofuels Directive. It also takes into account some elements of the recently adopted Renewables Directive. However, Croatia will not be able to achieve its 2010 target for electricity production from incentivised renewable energy sources. Alignment with the *acquis* in the area of RES is advanced but substantial efforts will be required if Croatia is to achieve the necessary concrete results.

Progress has been made in the field of **energy efficiency**. Legislation on energy end-use efficiency has been enacted. A National Energy Efficiency Action Plan has been prepared. Progress has been made in the transposition of the *acquis* relating to the energy performance of buildings with the adoption of implementing legislation on auditing the energy certification of buildings. Croatia still needs to ensure compliance in the area of high-efficiency cogeneration (CHP) and energy services. Alignment with the *acquis* is advanced. Administrative capacity in both energy efficiency and RES needs significant strengthening.

Good progress has been made in the field of **nuclear safety and radiation protection**. Implementing legislation relating to the provision of funds to cover Croatia's liabilities concerning the decommissioning of the Krško Nuclear Power Plant, including the disposal of radioactive waste and spent nuclear fuel, has been adopted. Croatia adopted in July 2009 a Nuclear Waste Management Strategy 2009-2019 covering the management of operational waste, decommissioning waste and spent fuel.

A new organisational structure for the State Office for Nuclear Safety, and actions to further align the legislation on radiation protection with the *acquis*, are under way. In addition, the Government adopted in July 2009 a document committing Croatia to streamline administrative structures responsible for nuclear safety and radiation protection to strengthen the efficiency and independence of operations. However the role of the Ministry of Health and Social Welfare in the inspection of facilities and devices generating ionising radiation needs to be clarified.

The licensing of a new facility for the storage of institutional radioactive waste remains a key safety issue that needs to be addressed by the Croatian authorities.

Conclusion

There has been good progress in this chapter. Overall, alignment with the *acquis* is well advanced. Efforts are still needed for adequate implementation of the priorities related to the functioning of the electricity and gas markets and for the promotion of renewable energy sources, particularly in view of meeting the EU's 2020 RES target. Further efforts are also needed to further empower and improve the functioning of the regulatory authority.

4.16. Chapter 16: Taxation

Some progress can be reported in the area of **indirect taxation**. Croatia's adopted a new VAT law which is significantly increasing the level of alignment with the *acquis*. Further efforts in this area are needed, in particular with regard to the scope of the reduced rates and of exemptions, the exclusion of free zones from the tax territory, and adding provisions for special schemes for travel agencies and investment gold. On excise duties, Croatia finally introduced a single rate of excise duty for cigarettes as from 1 June 2009, thus complying with its obligations under the SAA; a new Excise Act was adopted in July 2009, improving significantly the level of alignment with the *acquis*. However, further alignment of the excise legislation remains necessary, notably with regard to chargeability of duty on coal, gas and electricity, minimum rates and small producers. The provisions applicable to car taxation have to be aligned with the *acquis*.

Good progress has been made in the area of **direct taxation**. The Act amending the Profits Act has transposed EU Directives 90/434/EEC, 90/435/EEC and 2003/49/EC, with entry into force as from the date of Croatia's accession to the EU.

Good progress can also be reported on **administrative cooperation and mutual assistance**. Following the adoption of the Act on the Personal Identification Number, a single tax identification number for taxpayers has been established since 1 January 2009 and will be used for exchanging tax information. Croatia has transposed the EU legal framework for administrative cooperation with EU Member States, with entry into force as from the date of accession. The preparations for putting into operation of the Central Liaison Office (in the Tax Administration) and the Excise Liaison Office (in the Customs Administration) are very advanced.

There was some progress with **operational capacity and computerisation**. The Tax and Customs Administrations have continued working on IT interconnectivity projects to develop the mandatory VAT Information Exchange System and the Excise Movement Control System, completing the first phase of development for both systems. Attention should be given to reinforcing the IT capacity of the tax and customs administrations, which remain dependent on external expertise in IT matters.

Conclusion

Good progress was made in this chapter, not least on legislative alignment. The abolition of differentials in excise duties on cigarettes has eliminated all discriminatory elements, thus bringing full compliance with the SAA. Taking into account the provisions which were adopted but will enter into force upon accession, the legislation in the field of direct and indirect taxation has been aligned to a large extent with the EU *acquis*. Nevertheless, efforts are still required to align Croatian legislation, most notably in the field of VAT, where significant discrepancies remain. Efforts need to continue to strengthen administrative capacity, including IT interconnectivity.

4.17. Chapter 17: Economic and Monetary Union

Significant progress can be reported on alignment with the *acquis* governing **monetary policy**. Good progress has been made regarding the elimination of the legislative provisions granting public authorities privileged access to financial institutions. Overall, preparations in the field of monetary policy remain well on track, but more remains to be done to consolidate the independence of the Central Bank in the Constitution.

In the area of **economic policy**, Croatia has made some progress regarding alignment with the *acquis*, particularly in improving the institutional and technical capacity for setting up medium-term macroeconomic and fiscal frameworks. The Pre-accession Economic Programme (PEP) 2009-2011, submitted in January 2009, presented a sufficiently comprehensive and consistent macroeconomic and fiscal framework for economic policies. Due to the rapidly changing external environment, it retained only limited relevance as a core document for economic policy-making. Considerable further efforts were undertaken to bring fiscal reporting to ESA95 standards, although weaknesses remain. Broad political consensus on the essentials of a market economy has been maintained. Transparency on policy-making was enhanced through the establishment of the Economic Council. However, an ad hoc approach to economic policies has often continued to prevail. Overall, consensus on the fundamentals of a market economy has been maintained, but Croatia lacks a medium-term structural reform strategy.

Conclusion

There has been significant progress in the area of economic and monetary policy. Overall alignment with the *acquis* in this area is very advanced. However, work on anchoring the independence of the

central bank in Croatia's legislation needs to be completed. Further efforts are required concerning policy coordination.

4.18. Chapter 18: Statistics

Good progress can be reported concerning the **statistical infrastructure**. A new organisational structure of the Central Bureau of Statistics (CBS) has been adopted by the Government. This will increase the number of posts. The staff increase will focus on key areas such as agricultural and business statistics. The Act on Official Statistics has been amended with the aim of integrating the regional statistical offices into the CBS structure. This will increase efficiency of data collection. The Accession Partnership priority has been met. In addition the objectives of the statistical master plan have been so far achieved. A dissemination strategy of statistics is being developed. The situation in the IT department has somewhat improved. Preparations in this area are well on track.

Progress can be reported in the field of **classifications and registers**. Implementation of the NACE Rev.2 classification has started. The coverage and quality of the business register is being improved. Preparations in this field are on track.

Significant progress has been made in the area of **sector statistics**. Substantial progress has been made in the area of agricultural statistics, in particular with a view to obtaining comparable agricultural structure, agromonetary and animal production data. In the area of macro-economic statistics, a major revision has been completed, representing a significant step towards aligning Croatia's national accounts with EU standards. Key national accounts indicators and the methodology used are now largely in line with the *acquis* (ESA 95). Revised GDP figures have been published. These are, together with agricultural statistics, key elements for the accession negotiations on this chapter. The structural business statistics are being revised with the objective of providing data on all sectors, including at regional level. However, in social statistics, the Survey of Income and Living Conditions (SILC) is not yet implemented on an annual basis. Preparations in this area are well advanced.

Conclusion

Substantial progress has been made on modernising the statistical infrastructure. A good level of legal alignment has been reached. However, efforts should continue to further align Croatian statistics with EU requirements.

4.19. Chapter 19: Social Policy and Employment

There has been some progress in the area of **labour law**. Administrative capacity has been somewhat strengthened in the Directorate for Labour and the Labour Market of the Ministry of the Economy, Labour and Entrepreneurship (MoELE) as well as in the State Inspectorate. Work is underway to make the Wage Guarantee Agency operational and to establish a liaison office for posting of workers within the MoELE. However, in general, a number of shortcomings continue to persist as regards legal alignment and administrative capacity. The amendment of the Labour Act is still outstanding. This is a key element for the accession negotiations on this chapter. Preparations in this area are on track.

Good progress can be reported in the field of **health and safety at work**. Further amendments to the Occupational Safety and Health Act have been adopted with the aim of completing legal alignment. This is a key element for the accession negotiations on this chapter. A National Programme for Occupational Health and Safety 2009–2013 has been adopted. Implementation and enforcement capacity has substantially improved. The Institute for Occupational Health has been

restructured and now operates in new premises as the Institute for Health Protection and Safety at Work. The capacity of the Institute for Occupational Health and Safety Insurance has been substantially strengthened through an increase of staff from 32 to 111. The State Inspectorate has moved to new premises and has adequate management structures, as well as systems to recruit, train, appoint, authorise and monitor inspection staff. Recruitment of labour inspectors has continued, and attention has been paid to the mobility of the Labour Inspectorate. Preparations in this area are well advanced.

As regards **social dialogue**, there has been some progress. Tripartite social dialogue continues to be relatively well developed, and the influence of social dialogue on the decision-making process and policy design has continued to improve. Sectoral social dialogue has improved: there are now seven sectoral agreements signed. However, representativeness criteria for participation of trade unions in collective bargaining have not been adopted yet and bipartite social dialogue is not yet sufficiently developed. Also, the capacity of social partners continues to be somewhat weak. Preparations in this area are on track.

Progress has been made in the area of **employment policy**. Two Joint Assessment of Employment Policy Priorities (JAP) follow-up conferences have been held. A National Employment Plan (2009–2010) and the first Follow-up Report on the implementation of the JAP have been adopted, providing the basis for launching a new cycle of active employment measures. An anti-recession package has been adopted. As it does not directly focus on the labour market, it can be expected to have only a limited effect on unemployment. The low employment rate remains a concern, as well as rates for youth and long-term unemployment. (*see also section on economic criteria*). The link between the supply of human resources by the education system and demand on the part of the labour market is weak, and skills forecasting remains to be strengthened. Also regional disparities and the mismatch between demand and supply of labour are still considerable, although they are being adequately addressed. Preparations in this field are on track.

There has been significant progress in the preparations for the **European Social Fund**. The Operating Structure responsible for the Operational Programme for IPA component IV (Human Resources Development) has been established and accredited by the European Commission. Workload analysis and training plans for 2009–2010 are being developed. The current structure will be responsible for managing future implementation of the ESF. This is a key element for the accession negotiations on this chapter. Preparations in this field are well on track.

Good progress can be reported in the field of **social inclusion**. A third Joint Inclusion Memorandum (JIM) follow-up seminar was held in Zagreb. Governance, partnership and visibility of the JIM follow-up process for all stakeholders has been substantially reinforced. Preparations in further analysing community-based services and supporting innovative models of social services are ongoing. However, progress in the field of administrative and fiscal decentralisation of social services has been more limited and there is still a need to develop proper certification and accreditation system for social service providers. Continued progress can be reported in the process of de-institutionalisation for particular targeted groups, namely elderly, while progress for children and children with disabilities has been limited. The use of a coherent monitoring and evaluation system to assess policy reforms in this field remains to be strengthened. In general, overall progress in meeting the priorities and implementing the measures set out in the JIM document is slowly improving. As regards administrative capacity, the position of the Director of the Department for Social Welfare at the Ministry of Health and Social Welfare has been filled. Concerning people with disabilities, the office of the Ombudsman for Persons with Disabilities has become functional with an adequate number of staff. Accessibility to new buildings under construction has improved. Government cooperation with civil society organisations to create an adequate network of

community-based services has improved. However, budgetary constraints continue to limit the scope of the rights of people with disabilities to health and special care and their social integration (*see Political criteria — Economic and social rights*). Preparations in this area are on track.

Some progress can be reported in the field of **social protection**. Reforms in the pension and health care systems are ongoing. The monthly social welfare benefit has increased. Preparations for the development of a concept and strategy for social housing for the most vulnerable groups are ongoing. However, universal coverage and adequacy of pensions is not yet ensured. Poverty among the elderly as well as the large number of women of pensionable age not receiving pensions remain a concern, even if social pensions are foreseen for these categories by 2011. Preparations in this field are on track.

There has been good progress in the field of **anti-discrimination**. The Ombudsman's office has been transformed into an independent Equality Body. Administrative capacity has been strengthened for this purpose by bringing the number of staff from 16 to 31. Awareness-raising activities in this area are ongoing. However, some aspects of the level of protection against discrimination in practice and the judicial prosecution of acts of discrimination are still being brought in line with EU standards.

Vulnerable groups and ethnic minorities, particularly the Serb and the Roma minorities, continue to face discrimination in economic and social life (*See Political criteria — Economic and social rights*). The limited statistics currently available still do not allow monitoring of discrimination on different grounds, as required by the *acquis*. Development of a system for statistical monitoring of discrimination cases has started, but is facing budgetary constraints. Preparations in this field are on track.

Good progress can be reported on **equal opportunities**. The office of the Ombudsman for Gender Equality has been transformed into an independent Equality Body. However, budgetary constraints have put at risk the necessary staffing to monitor the relevant legislation. County commissions have been established with the task of monitoring the implementation of the Gender Equality Act at local and regional levels. Awareness-raising activities on gender equality have continued in different areas. However, effective implementation of the National Policy for the Promotion of Gender Equality is not entirely ensured (*see Political criteria — Economic and social rights*). Preparations in this field are well advanced.

Conclusion

Good progress has been made on this chapter. Overall, a good level of legal alignment has been reached although some gaps remain, especially as regards labour law. Strengthening the administrative capacity in good time before accession to ensure proper implementation and enforcement of the *acquis* in this field remains the key element for the accession negotiations on this chapter.

4.20. Chapter 20: Enterprise and Industrial Policy

Some progress can be reported in the field of **enterprise policy**. Croatia continues to implement the actions and guidelines of the European Charter for Small Enterprises. Steady progress was made in entrepreneurial learning activities and enterprise skills development. A Public-Private Dialogue Committee was established under the umbrella of the Ministry of the Economy, Labour and Entrepreneurship (MELE). It is meeting regularly which represents a significant progress. Croatia participated in the activities of the European SME Week.

Steady progress was made in entrepreneurial learning activities and enterprise skills development, through plans for more developed and systematic intelligence on human capital within enterprises.

Further efforts were made to strengthen the SME Development Agency (HAMAG) and to refine its role vis-à-vis that of the MELE, but cooperation between the two authorities remains to be improved. Although good results were achieved in the implementation of the SME policy, MELE's role as SME policy coordinator at government level remains to be strengthened.

However, regulatory impact assessment (RIA) is not applied to new legislation on the business sector. A department for RIA in the MELE remains empty. Furthermore, the central coordination office for RIA closed in August due to budgetary constraints, bringing the RIA implementation to a halt. There are no developments regarding the silence-is-consent principle. The impact of the financial crisis is amplifying some issues such as illiquidity, particularly due to delays in payments by public companies and institutions.

Croatia completed the review of the current legislation concerning the business environment, as part of the 'regulatory guillotine' process, and made progress in streamlining and eliminating unnecessary legislation. However, efforts are still needed in this area.

As regards the business environment, some progress has been made in speeding up company registration through online registration (*See Chapter 6 — Company law*). However, over-regulation, numerous para-fiscal taxes, an inefficient judiciary and public administration as well as petty corruption all severely hamper the business environment.

Croatia made good but uneven progress on **enterprise and industrial policy instruments**. Croatia is an active member of the Enterprise Europe Network and participates in all three pillars of the Community Programme CIP. The alignment of Croatian legislation with the Directive on combating late payments is still not completed.

There has been some good progress in the field of **sectoral policies**, especially as regards shipbuilding. In the steel sector, the implementation of the national restructuring programme (NRP) has been disrupted by the economic crisis. As a result, the individual business plans and the NRP will have to be revised (*see Chapter 8 — Competition policy*). Further progress was achieved in improving the strategic and legal framework in the field of tourism.

Conclusion

Some progress was achieved on this chapter. Overall, alignment with the *acquis* in this chapter is very advanced. However, further efforts are needed to put into practice the regulatory impact assessment of new legislation. The current pace of reforms to improve the business and notably the SME environment should continue in line with the Small Business Act. Further efforts are required in the steel and shipbuilding sectors.

4.21. Chapter 21: Trans European Networks

There has been good progress in the development of **transport networks**. Croatia has continued to actively participate in the implementation of the 2004 Memorandum of Understanding on the development of the South East Europe Core Regional Transport Network and in the South East Europe Transport Observatory, particularly by updating and implementing the Multi-annual Plan 2009-2013.

Croatia and the European Commission came to an agreement on the future Croatian TEN-T network and priority projects of European interest in the framework of this network. This will be the focus of future Croatian investments in upgrading the relevant infrastructure to the TEN-T standards. Further infrastructure upgrades have been made towards this aim during the past 12 months. The Trans-European Network in Croatia will consist in a multimodal network including main road, rail, inland waterway, river port, seaport and airport infrastructures in the country.

As regards **energy networks**, Croatia has continued to be active in developing interconnections between its electricity network and those of neighbouring countries and EU Member States.

There has been progress on telecommunications networks. The Memorandum of Understanding between the Republic of Croatia and the European Community on the participation of the Republic of Croatia in the Community Programme 'ICT Policy Support Programme (ICT PSP) of the Competitiveness and Innovation Framework Programme (2007 to 2013)' has been in force as of 2008 and Croatia has become a full member of the ICT PSP.

Conclusion

Croatia has made good progress regarding the development of its transport and energy networks in line with the design and objectives of the TEN–Transport network and TEN–Energy network. Overall, alignment with the *acquis* is well advanced.

4.22. Chapter 22: Regional Policy and Coordination of Structural Instruments

There has been some progress with regard to the **legislative framework**. The new Budget Law entered into force in January 2009. This law introduces multi-annual budgetary planning and budget flexibility, desirable in relation to regulatory requirements of Community cohesion policy. It does away with the limit on the borrowing capacity of local self-government units for co-financing of EC projects. It is a tool that will contribute to clear coordination between the Ministry of Finance (MFIN) and the Central State Office for Coordination of EU Funds (CODEF) on the preparation of the three-year Government Programmes Strategy. There was also progress in alignment with Community legislation in other areas: public procurement (concessions and PPPs); competition, State aid and the environment. Croatia needs to ensure that all relevant legislation and strategies in the context of regional development are fully in line with the EC cohesion policy framework and negotiations under this chapter. Preparations in this area are fairly advanced.

There has been good progress with the **institutional framework**. The Commission conferred management powers on the relevant Croatian authorities for IPA (Instrument for Pre-Accession Assistance) components II (CBC), III (Regional Development) and IV (Human Resources Development), all precursors of the Structural Funds. Croatia needs to legally formalise the institutional set-up for managing structural instruments, building on the existing system. This is a key element for the accession negotiations in this chapter. Preparations in this area are moderately advanced.

There has been some progress in the area of **administrative capacity**. Croatia has undertaken a systematic analysis of the organisational, staff and training needs for IPA and the Structural Funds and is preparing Organisational Development Strategies for all key bodies involved in cohesion policy management and/or implementation. An overall Institution Development and Capacity Building/Training Strategy is being prepared. This is one of the key elements for the accession negotiations in this chapter. Croatia needs to further strengthen considerably its administrative capacities in the implementation of pre-accession funding under Phare/ISPA and IPA. This includes the availability and retention of adequate qualified and trained staff in existing IPA structures for

which a structural solution is necessary. Particular effort is also needed in ensuring proper management and coordination of various ongoing (and planned) technical assistance actions and training activities aiming at enhancement of administrative capacity. Administrative capacity needs to be significantly increased in order for Croatia to achieve absorption under IPA and the future Structural Funds. Preparations in this area are not very advanced.

Progress has been made with respect to **programming**. Croatia has completed programming under IPA, including submission of Operational Identification Sheets for components III and IV. The drafting and consultations for the National Strategic Reference Framework have started. A coordination body for the National Strategic Reference Framework under the Central State Office for Development Funds (CODEF) was established and analysed a first draft of the document. The accompanying operational programmes are also being prepared. This is one of the key elements for the accession negotiations in this chapter.

However, in the programming documents Croatia will have to demonstrate that national and sectoral strategies have been incorporated and that relevant Ministries have full ownership of the programming process. Croatia needs to further its efforts in addressing the coordination and quality participation of all stakeholders during the preparation of programming documents. It needs to significantly increase its efforts towards preparing a comprehensive and quality project pipeline for implementation of IPA as well as for the Structural Funds/Cohesion Fund. Particular efforts are needed to prepare sufficient number of good quality and mature projects in the environment and transport sectors. As regards the Structural Funds, the identification of projects has only started and project preparations are still at a very early stage. Preparations in this area are advancing slowly.

There has been good progress in the area of **monitoring and evaluation** of the IPA operational programmes. The third and fourth regular sectoral monitoring committee (SMC) meetings to monitor implementation of the OPs took place in December 2008 and June 2009. The respective Operating Structures have satisfactorily prepared and co-chaired the SMC meetings. The second meeting of the joint IPA Monitoring Committee (all components) was held in July 2009. Croatia has also begun addressing its needs for establishing monitoring and evaluation systems for the Structural Funds. It has prepared a plan and timetable for setting up a monitoring and evaluation system, including its electronic monitoring system (MIS). This is a key element for negotiations under this chapter. The Croatian authorities are currently testing the functioning of the electronic monitoring system (MIS) for IPA III and IV. Croatia plans to build on its IPA MIS to meet the requirements of the MIS for the Structural Funds. Croatia needs to formulate technical specifications and obtain technical assistance for setting up its system to meet the requirements of the Structural Funds. Preparations are making good progress.

Some progress can be reported in the area of **financial management and control** (*see also Chapter 32 — Financial control*). The Croatian National Fund (Ministry of Finance) has submitted draft roadmaps for waiving ex-ante controls under IPA, under which financial management and control systems are to be strengthened. However, Croatia still has a long way to go in establishing its financial management and control systems for the future Structural and Cohesion Funds. Croatia needs to build up its capacity in these fields. Preparations in this area are advancing.

Conclusion

Some progress has been made under this chapter, notably in preparing implementation of those IPA components which serve as pre-cursors to the Structural Funds. Croatia is partially aligned with the acquis. Further efforts are needed to meet the regulatory and operational requirements stemming from the Community's cohesion policy. Croatia needs to complete its institutional set-up for the

Structural Funds/Cohesion Funds. It needs to substantially increase administrative capacity in existing IPA structures and adequately prepare them for the future. The project pipeline for both IPA and the Structural Funds needs to be strengthened to ensure absorption of funds. Programming of the National Strategic Reference Framework and Operational Programmes for the Structural Funds needs to be undertaken in a quality and timely manner. Financial management and control systems as well as an effective MIS need to be set up for the Structural Funds.

4.23. Chapter 23: Judiciary and fundamental rights

There has been some progress in the area of the **judiciary**.

As regards the *independence of the judiciary*, there has been some progress. An amended Law on Trainees in Judicial Bodies and the Bar Exam entered into force in January 2009. This law introduces an improved selection procedure whereby candidates are ranked by points based on various criteria. The bar exam has also been made more practice-oriented.

However, the selection procedure for judges and prosecutors remains deficient, lacking transparency and the application of uniform, objective criteria. A strategic study adopted by the government in December 2008 proposes the introduction of a competitive exam for entry to a new school for judicial officials. However the relevant legislation has not yet been passed. Particular attention will be needed to see that the selection procedure ensures the constitutionally guaranteed independence of the judiciary.

The Courts Act amended in October 2008 introduced the obligation on the Minister of Justice to conduct preliminary interviews in the procedure of appointing presidents of courts. While the declared aim to focus on managerial competence is laudable, the involvement of the Minister of Justice in the appointment of the presidents of courts as such remains problematic from the point of view of judicial independence. A clearer separation between administrative and judicial functions should be strived for.

The five-year probation period for judges remains in place. The provisions on penal immunity for judges have also not been changed in order to ensure transparency and accountability within the judiciary.

As regards the *impartiality* of the judiciary, the State Judicial Council has continued to conduct disciplinary proceedings initiated by court presidents and the Ministry of Justice. In 2008, there were eleven disciplinary proceedings resulting in one reprimand, one fine and one dismissal of a judge. Eight cases are ongoing. However, disciplinary proceedings against attorneys and judges continue to lack transparency. There are still no means for the Ministry of Justice to systematically check the accuracy of declarations of assets by judges and prosecutors.

The appointment procedures for the State Judicial Council (SJC) and the State Prosecutorial Council (SPC) should be reviewed in order to ensure their independence and to reduce the potential for political interference. The SJC does not currently have sufficient capacity to carry out its key functions.

Some progress has been made as regards *professionalism and competence* in the judiciary. The Judicial Academy continued to carry out its in-service professional training programme. Initial training programmes for judicial trainees and advisers started in April 2009. However, initial training for future judges and prosecutors is still missing. Administrators have been recruited for each of the regional centres, but the Judicial Academy remains understaffed, without either permanent premises or an adequate budget to perform its duties.

Progress has been made in relation to the *efficiency of the judiciary*. The backlog of cases was further reduced by 8.4% to 887,000 in December 2008. Good progress was made on reducing the number of old civil and criminal cases by 31% and 52% to 102,430 and 4,408 respectively. In addition, the new Law on Misdemeanours, the new Civil Procedure Code, and the amended Law on Courts seem to have contributed to reducing the inflow of new cases into courts. Thanks also to the use of accelerated procedures the number of pending misdemeanour cases was reduced by about one third.

However the overall backlog as well as the number of unresolved cases older than 3 years remains high. Without more far-reaching reform, continued reduction of the backlog may not be sustainable, especially if judges have focused on 'easier' cases to meet output targets. Moreover, problems with the enforcement of court rulings constitute a major obstacle to the efficiency of the judicial system. The number of enforcement cases in the backlog remains high. Reform of the enforcement procedure remains long overdue, although a strategic study on enforcement was adopted in July 2009 which foresees the introduction of a new system of enforcement officers. There is still no unified statistical system of case management in the judiciary.

Special chambers for dealing with organised crime and corruption cases (USKOK cases) have been set up in the four County Courts in Zagreb, Split, Osijek and Rijeka. The 60 judges that will work in these chambers have not been relieved of their previous duties. This suggests that the much warranted increased focus on cases of organised crime and corruption may come at the expense of other categories of cases.

The handling of *administrative cases* continues to face particular challenges. Finalisation of the Law on Administrative Court Disputes has been delayed. The Administrative Court still needs to be made a court of full jurisdiction in the meaning of Article 6 of the European Convention on Human Rights.

There has been some progress in the *rationalisation of the court network*. As of January 2009, the number of municipal courts was formally reduced from 108 to 67. However, so far only six municipal courts have been physically merged into three courts. A laws regulating the reduction in the number of State Attorney's Offices from 71 to 55 has also been adopted. The draft law foreseeing the reduction in the number of misdemeanour courts from 114 to 61 has been pending approval in parliament for one year. A new department supervising the rationalisation process has been set up in the Ministry of Justice. However, this department is understaffed and it remains unclear how court rationalisation will be financed and implemented in practice. The timetable for physical mergers remains unclear and unambitious. No steps were taken to rationalise the county courts and commercial courts.

With regard to the *infrastructure and equipment of courts*, there has been limited progress. The integrated case management system (ICMS) is running in nine courts and a special case tracking system was also developed for prosecution offices. However, the planned rollout of the ICMS to the other courts is still behind schedule. Misdemeanour courts continue to suffer from a shortage of equipment and a very low standard of premises.

The system of *judicial inspections* has shown good results. The Ministry of Justice has reinforced the inspection team with twenty part-time inspectors for all types of courts. In 2008 about eleven inspections were performed resulting in the removal of the two court presidents, disciplinary procedures and internal court reorganisation. However, staff shortages have led to few inspections being carried out in 2009. The prosecution offices remain outside the scope of the judicial inspections. No information is available on their internal inspections.

The new *Criminal Procedure Code* was adopted in December 2008. The new law substantially modifies the judicial investigation, transferring competence from the investigative judge to the State Prosecutor, in close cooperation with the police. While training measures for judges, police and prosecutors have begun, several regulations and the provision of further training are still required for full entry into force of the new Code. The new provisions apply from July 2009 for organised crime and corruption cases and as of 2011 for other cases.

The use of *alternative dispute resolution* has continued. The new Civil Procedure Code has introduced mediation centres in all first instance courts, adding to the mediation possibilities in the commercial courts and in eight municipal courts. The law on mediation amended in June foresees improvements in the independence and competence of mediators. However, the high number of mediation cases is burdening the courts, resulting in delays and backlogs. In addition the new civil procedure code excludes the possibility of referral by a judge to an out-of-court mediation centre. The mediation strategy adopted in May 2009 does not focus sufficiently on out-of court mediation. Further streamlining of court procedures is necessary.

Implementation of the *judicial reform strategy* has continued. A large volume of new legislation was adopted. The Ministry of Justice was reorganised and the directorate for strategic development reinforced. However, adequate monitoring of reform measures has not been possible due to continued limits on administrative capacity. There is only limited assessment of the impact of new measures. Legislation is often amended on such a regular basis that reforms do not become properly embedded in the system. Post-legislative scrutiny is practically non-existent.

(See also 2.1. Democracy and Rule of law)

There has been some progress in the **fight against corruption**. Implementation of the anti-corruption strategy and related action plan has continued. The legal framework to combat corruption has been further improved. Amendments to the Criminal Code introduced new rules on confiscation of assets. From now on, where the origin of certain assets held by persons convicted for organised crime or corruption is in question, the burden of proof is reversed. The National Council for monitoring the anti-corruption strategy has become more proactive, regularly holding public debates and hearings. A national anti-corruption campaign for the general public was launched.

A National Police Office for the Suppression of Corruption and Organised Crime (PNUSKOK) has been established within the General Police Directorate. It comprises four regional centres, in line with the structure of the Office for the Fight Against Corruption and Organised Crime (USKOK), and is in charge of complex police investigations and actions against organised crime and corruption at the national level. Special chambers for dealing with organised crime and corruption cases have been set up in the four County Courts in Zagreb, Split, Osijek and Rijeka.

The Office for the Fight Against Corruption and Organised Crime (USKOK) continues to be increasingly active. It has begun to investigate possible high level corruption, initiating an investigation of a case involving a former government minister. USKOK has issued indictments in some other important cases. It issued an indictment against a High Commercial Court judge and a judge from the Zagreb Municipal Court for corruption and abuse of power. Further indictments were issued in the 'Indeks' case concerning corruption at universities, including against a deputy dean of the Zagreb Faculty of Transport and Traffic Engineering and nine professors. There have been the first verdicts in some important cases brought by USKOK. In the second 'Maestro' trial, the Zagreb County Court issued at the first instance prison sentences against two former vice-presidents of the Croatian Privatisation Fund (HFP).

However, corruption still remains widespread. The recently upgraded legal and administrative structures remain to be tested in practice. While the total number of corruption cases investigated so far has increased, the actual number of prosecutions remains low. The ratio between investigated cases and indictments also remains low. There has been limited investigation of high-level corruption, the prosecution of which is frustrated by political considerations. There are indications that indictments are often overly narrow and unambitious. A culture of political accountability for the corruption being uncovered by USKOK is lacking.

The administrative capacity of State bodies for fighting corruption continues to need improvement. Overall coordination of the implementation of anti-corruption efforts has improved but still faces shortcomings. Further administrative support needs to be provided to both the National Anti-Corruption Council and the Committee for the Prevention of Conflicts of Interest (CPCI). There has been limited progress in preventing conflicts of interest. The CPCI was re-established after a period of interruption but has not secured a strong preventive role for itself. While the CPCI has issued guidelines for public officials, the concept of conflict of interest remains little understood or wilfully ignored across the wider public administration. Efficient non-partisan monitoring of anti-corruption efforts is still to be established. Serious implementation of anti-corruption practices by the public administration is lacking, with many bodies only paying lip service to the centrally coordinated anti-corruption drive.

On the prosecution front, in order to be able to conduct complex financial investigations USKOK as well as PNUSKOK need to improve their expertise on financial issues as well as further enhance their cooperation with other bodies. In order to prevent corruption, greater transparency in public administration is required. Shortcomings remain as regards the financing of political parties and election campaigns. Implementation of the Law on Access to Information needs further improvement. Public procurement remains a major source of potential and actual corruption. In view of future EU funds to be allocated to Croatia after accession, particular attention to fighting corruption in this area is required. Significantly improved scrutiny of actual execution of contracts is essential

(See also 2.1. Democracy and Rule of law)

As regards **fundamental rights**, there have been some developments.

As regards the right to *protection of personal data*, the Data Protection Agency has been further strengthened with additional staff to cover new activities such as Schengen and Eurojust. The number of supervision and control activities remains low, however. Full alignment with the Data Protection Directive and the Council of Europe instruments remains to be completed.

Some progress was made as regards *prisons*. The Law on Enforcement of Prison Terms was adopted in 2008, providing for the expansion of existing facilities and improved health care. 171 additional staff were recruited and trained. However, Croatian prisons remain overcrowded, with the number of detainees increasing due to longer prison sentences introduced in the Criminal Code. As an alternative to imprisonment, a probation system should be introduced. There is a lack of trained prison staff.

Freedom of expression, including freedom and pluralism of the media, is provided for in Croatian law and is generally respected. However, there has been an increase threats against journalists working on cases of corruption and organised crime. There has been limited success in identifying and prosecuting perpetrators and instigators. Undue political pressure is on occasion exerted on editors and journalists. Concerns about freedom of expression persist, including at the local level.

As regards access to justice, the new Law and implementing regulations on *legal aid* entered into force in February 2009. The institutional framework set up for implementation of the law comprises a Department for Free Legal Aid within the Ministry of Justice, 20 State administration offices in counties and 13 branch offices as well as a Legal Aid Commission. The system remains to be fully tested in practice. However, the complexity of the procedure, low fees for lawyers relative to their normal tariffs and the significant reductions in the budget for legal aid provision might not guarantee proper access to justice.

There has been some progress with regard to *minorities*. High-level public expressions of commitment to the rights of minorities, reaffirming their place in Croatian society, have continued. All eight minority MPs remain in the governing coalition. The Roma minority has continued to receive attention, with improvements particularly in pre-school education. Round tables and public discussions have been held on the Constitutional Law on the Rights of National Minorities (CLRNM), in particular concerning minority employment in the State administration and judiciary.

However, many problems remain for minorities. Croatia needs to encourage a spirit of tolerance towards the Serb minority and take appropriate measures to protect those who may still be subject to threats or acts of discrimination, hostility or violence. Minorities continue to face particular difficulties in the area of employment, both in terms of under-representation in State administration, the judiciary and the police as well as in the wider public sector. Implementation of the recruitment plan for national minorities has not seen a significant increase in minority employment in the State administration. Funding for minorities was cut in the revised budget. Legal provisions and programmes need to be implemented with more determination, and adequate monitoring assured, especially in the area of employment.

The Roma minority still faces particularly difficult living conditions and challenges remain in the areas of education, social protection, health care, employment and access to personal documents.

There has been some progress on refugee return issues. The government's self-imposed 2007 benchmark for the provision of housing care to former occupancy and tenancy rights holders has been met. Good progress has been made towards meeting the 2008 benchmark of providing 1,400 accommodation units; though this remains to be fully met. Work on meeting the 2009 target is still at an early stage. Several thousand housing units still need to be made available to returning refugees. Moreover, some 8,000 appeals for housing reconstruction still remain pending. Implementation of the decision on validating pension rights has been varied. The current rejection rate of over 50% of applications and inconsistent approach by regional offices mean that in practice people are often not able to avail themselves of their rights. Efforts to create the economic and social conditions necessary for the sustainability of refugee return need to be accelerated.

As regards **citizens rights**, Croatia has amended the Act on Aliens to align with Directive 2004/38/EC on the right of citizens of the Union and their family members to move and reside freely within the territory of the Member States but further efforts are required to achieve full alignment.

(See also 2.2. Human rights and the protection of minorities)

Conclusion

Croatia has made some progress on this chapter. Reforms in the judiciary have continued but significant challenges remain, particularly concerning judicial independence and efficiency. Anti-corruption efforts have produced initial results, but corruption remains widespread and tools are not being deployed with sufficient vigour, especially against political corruption. Legal provisions on

fundamental rights are in general adequate, but despite some progress, a number of important challenges remain in terms of implementation, especially for minorities. Particular vigilance is required as regards freedom of expression and threats against journalists.

4.24. Chapter 24: Justice, Freedom and Security

In the field of **migration**, amendments to the Aliens Act facilitate family reunification for persons under subsidiary protection. There has been no increase in the number of staff at the Ministry of the Interior dealing with illegal migration. Training of existing staff has continued. A Memorandum of Understanding was signed in November 2008 between Albania, Bosnia and Herzegovina, Croatia, the former Yugoslav Republic of Macedonia, Montenegro and Serbia with a view to establishing a system for the exchange of statistical data on illegal migration and participating in a regional early warning system.

The number of illegal migrants continued to fall (2,013 in 2008 compared to 4,000 in 2007) and, as a result, the number of forced returns decreased by 45% in 2008 as compared to the previous year. The deportation centre at Ježevo accommodated 773 illegal migrants waiting for deportation and did not suffer from overcrowding, as in previous years. There is a lack of specific treatment, including separate facilities, and protection for minors, who are subject to risks of abuse and exploitation. A readmission agreement with Montenegro was ratified in February 2009 and a readmission agreement with Serbia to bring it into line with the EU agreement has been signed.

Significant progress can be reported in the field of **asylum**. The practice of the authorities towards asylum-seekers has improved compared to previous years. However, the legislation needs to be brought fully into line with the *acquis*. An educational manual has been developed, continuous education of existing and newly hired staff (7 new staff) has been ensured, manuals for staff at the reception centre and for caseworkers at the Ministry of the Interior, as well as a Eurodac and Dublin implementation plan and operational manual have been prepared.

The number of asylum seekers decreased to 155 in 2008 from 170 in 2007. The majority of applications for asylum continue to be rejected as manifestly unfounded. The exclusion of interviews in the accelerated procedure remains a concern, even though in practice the Asylum Commission has so far interviewed all asylum seekers. The fact that the Asylum Commission overturned four first instance decisions taken by the Asylum Unit of the Ministry of the Interior can be considered as a positive sign. However, the Commission still lacks guarantees of full independence, given the oversight role of the authorities in the appointment process and the lack of separate premises from the Ministry. The Administrative Court (which can review decisions of the Asylum Commission) does not provide an effective legal remedy and cannot suspend an expulsion decision. The fact that asylum seekers continue to be charged with the offence of illegal entry remains a matter of concern. Recognised refugees face difficulties and discrimination in accessing their rights due to their status. The Kutina asylum reception centre is reaching its maximum capacity. Croatia is still perceived as a country of transit, but the situation is likely to change upon its accession to the EU and Croatia needs to build up its capacity to deal with this expected increase.

Some progress has been made as regards **visa policy**. As regards amendments to the positive and negative lists, the visa requirement for citizens from Serbia and Montenegro has again been suspended, until the end of 2009, and for citizens from Russia and Ukraine it has been suspended for the period 1 May to 31 October 2009.

Further amendments to the Aliens Act entered into force in March 2009 and introduced requirements for travel insurance and for collecting biometric identifiers. The latter of these

provisions are to enter into force upon accession to the EU. New Croatian visa stickers have been introduced in order to align with the acquis. IKOS, the information system which forms the basis of the future Croatian Visa Database, has now been implemented in all but two Croatia's diplomatic missions and consular posts. Croatia needs to prepare for the implementation of the Visa Information System.

Concerning document security, the legislation introducing biometric identifiers (facial image and fingerprints) in passports and travel documents has entered into force and the issuance of biometric passports started in July 2009 for diplomatic passports.

There has been some progress with regard to **external borders and Schengen**. The revised Integrated Border Management Action Plan was adopted in March 2009 together with a Strategy for Integrated Border Management. The Report of the Working Group proposing the reduction and re-classification of Border Crossing Points (BCPs) has been adopted and Croatia has started negotiating with neighbouring countries on such proposals. The total staff of the border police remained roughly at the same level as in the previous period, and remains insufficient since some BCPs are severely understaffed and surveillance activities are often suffering. Training of border police has continued and both basic and specialised training programmes have been established as well as training of trainers. The encrypted communication system (Tetra) now covers all Border Crossing Points.

Although some progress has been made, there is still a lack of equipment, notably for second-line checks, surveillance and for the detection of forged documents. Infrastructure in several BCPs is poor. The National Border Management Information System (NBMIS) is being deployed to BCPs at a slow pace and it still covers only 9 BCPs. Rollout of the NBMIS system should be speeded up to cover the whole border and prepare for the implementation of the national system for the Schengen Information System (SIS II). Croatia needs to finalise preparations for setting up a SIRENE Office. An Annex to the Agreement on Cooperation on Integrated Border Management has been signed to strengthen inter-agency cooperation.

Cross-border cooperation continues to work well. Since November 2008 Croatia and Bosnia and Herzegovina have been conducting joint patrols along some parts of the border. In December 2008, an annex to the working arrangement between FRONTEX and the Ministry of the Interior was signed on data to be exchanged between agencies. The implementation of the working arrangement has started and Croatia is participating in joint border control operations. The concept of a risk analysis system has been introduced but still needs to be developed.

As regards **judicial cooperation in civil and criminal matters**, there has been some progress. Croatia amended its Criminal Code in December 2008 to withdraw the exception to the *ne bis in idem* principle. The Law on Courts and the Law on Enforcement were amended in order to align with the European arrest warrant and the European enforcement order. However, central bodies have to be set up in the county courts and the Constitution has to be amended to allow extradition of Croatian citizens to EU Member States in order to complete alignment. Croatia is a party to the Council of Europe Convention on the Transfer of Sentenced Persons (1983), but it has not signed or ratified the Additional Protocol to the Convention (1997).

Regarding the status of victims in criminal proceedings, the Law on compensation of the victims of violent crimes was adopted in October 2008. However, Croatia has to align further with the Framework Decision on the standing of victims in criminal proceedings in a number of areas. These include notifying the injured party that the perpetrator has been released after serving the sentence, acquiring testimonies by means of devices for picture and sound transmission (video and phone

conferences), establishing a service for assistance to victims of criminal offences and training of staff. Croatia has not aligned with the Framework Decision on the execution in the EU of orders freezing property and evidence or with the Framework Decision on the application of mutual recognition of financial penalties. Croatia has not adopted the relevant legislation to be able to implement the Directive on combating late payment in commercial transactions. The Croatian legal order does not allow direct communication between judicial authorities, nor does it allow the direct execution of foreign decisions without the need for the *exequatur* procedure. This means, in practice, that recognition and enforcement of decisions by foreign courts has to go through the *exequatur* process at the municipal or commercial courts. The recognised decision is enforced according to Croatian law, which remains slow and inefficient. The Ministry of Justice has no statistical data on the recognition/enforcement of such decisions.

Concerning cooperation in civil matters, Croatia has signed and ratified the Convention on Jurisdiction, Applicable Law, Recognition, Enforcement and Co-operation in respect of Parental Responsibility and Measures for the Protection of Children but still has to ratify the Hague Convention on the Taking of Evidence abroad in Civil and Commercial Matters.

Good progress has been made as regards **police cooperation**. The agreement with Europol is being implemented and since a Croatian liaison officer was stationed at Europol last year there has been a significant increase in cooperation between Croatia and Europol. Agreements on police cooperation have been signed with Hungary, Germany and Serbia. Cooperation with Serbia has produced some important results, including identifying and arresting the alleged perpetrator of the killing in October 2008 of a prominent journalist in Zagreb. The Agreement with France entered into force.

A new Act on police duties was adopted in June 2009. The duties and powers of the police are extended and better defined. A Strategy and an Action Plan for reforming human resource management in the Ministry of the Interior for 2009-2011 was adopted.

Some progress has been made in the area of **organised crime**. The National Police Office for the Suppression of Corruption and Organised Crime (PNUSKOK) was established within the General Police Directorate and became operational in February 2009. It also comprises four regional centres in Zagreb, Split, Osijek and Rijeka. Based on the National Threat Assessment (NTA), the Ministry of the Interior developed a Plan of Priorities in the Suppression of Organised Crime, which it is implementing together with USKOK. An additional Protocol on inter-ministerial exchange of information from December 2008 specifies which data are to be exchanged. Good cooperation was established between the Ministry of the Interior and USKOK. Efforts in this respect need to be continued. In addition, Croatia will need to increase its efforts in meeting the challenge of illegal proceeds of the crimes being invested in society in a more developed manner, as well as the tendency of criminals using more sophisticated methods for money laundering.

Good progress has been made with regard to the **trafficking of human beings**. In November 2008, the government adopted a protocol for the identification of, assistance to and protection of victims of human trafficking which sets out in detail the national referral mechanism and the obligations of the various responsible authorities. A three-year programme to combat trafficking in persons was adopted by the government in March 2009.

As part of the implementation of the protocol on cooperation between the various Croatian authorities involved in the system of suppression of trafficking (adopted in June 2008), training was given to police officers, employees of the social welfare system and of family centres, health care staff, workers in tourism and representatives of civil society organisations (450 persons in total). Further efforts should be made in terms of identifying potential victims of trafficking and

developing a protocol for the return of victims of trafficking.

Progress can be reported in the **fight against terrorism**. In November 2008 Croatia adopted the National Strategy for the Prevention and Suppression of Terrorism, and the Act on the Prevention of Money Laundering and Financing of Terrorism entered into force in January 2009. Croatia has amended its legislation in order to align with the EU definition of terrorism. Training of police officers on anti-terrorism operations has continued. Croatia needs to continue to strengthen its administrative capacity in the fight against terrorism, among other things by developing inter-agency coordination.

Progress has been made in the field of the **fight against drugs**. In February 2009, the National Action Plan on drugs for the period 2009-2012 was adopted on the basis of the objectives set by the National Drug Control Strategy for 2006-2012. The Action Plan focuses on reinforcing cooperation between central and local levels as well as with civil society and enhancing the role of schools in the field of prevention. The National Focal Point (NFP) delivered its second Annual Report to the European Monitoring Centre for Drugs and Drug Addiction (EMCDDA) in December 2008 and was able to report on four out of the EMCDDA's five indicators. The NFP suffers from a shortage of staff and financial resources. Standards for therapeutic communities have been drawn up but the implementing legislation has not been adopted. The model for partnership cooperation adopted last year between the National Drug Office and the districts helped strengthen cooperation between central and local levels as well as exchanges of good practice amongst districts. Prevention programmes on drugs in general, and at schools in particular, lack quality evaluation to assess their impact. The police recorded 7,882 criminal cases involving drugs in 2008 (which is comparable with the level of each of the past six years). The agreement for Croatia's participation in the EMCDDA was initialled in July 2009. The agreement now needs to be ratified before Croatia can participate in the EMCDDA's work.

No progress can be reported in the field of **customs cooperation**.

For counterfeiting of the euro see chapter 32 – financial control.

Conclusion

Croatia has made some progress in this chapter, particularly as regards the fight against drugs, dealing with trafficking of human beings, and the management of external borders. However, Croatia needs to step up its efforts in order to ensure that EU requirements are met upon accession. Efforts to develop the necessary administrative capacity in this chapter require significant upscaling. Croatia needs to develop its infrastructure, equipment and resources to ensure the effective management of its external border as from accession.

4.25. Chapter 25: Science and Research

Good progress has been made in **research policy**. Amendments to the Act on the National Foundation for Science, Higher Education and Technological Development have been adopted, setting in place a transparent and independent system for evaluating and monitoring national research grants. An Act on Quality Assurance in Science and Higher Education has also been adopted assigning the Agency for Science and Higher Education an independent quality assurance role through the accreditation, evaluation and audit of public and private scientific and higher education institutions.

Good progress has been made on participation in the 7th **Framework Programme** for Research and Technological Development (FP7). An Action Plan to further strengthen Croatia's absorption

capacity for the period 2009–2010 has been adopted. Efforts are ongoing to strengthen administrative capacity, including further training of the appointed national contact points. Additional financial support has been made available for preparing EU projects and reward the successful Croatian applicants. The procedure to associate Croatia to the Seventh Euratom Framework Programme is ongoing with the aim of making the association effective in the course of 2010.

Progress has also been made with respect to Croatia's association to the **European Research Area**: implementation of the 'National 3% Action Plan' is regularly assessed and updated by the Council for the National Innovation System. Measures have been taken to stimulate private sector investment in research, including tax reliefs for private investment in research and development. Implementation of the Plan needs, however, to be ensured. As regards mobility of researchers, the Croatian Researchers' Mobility Network Euraxess has been established as well as local contact points. An Action Plan for the mobility of researchers has been adopted. However, the number of young people attracted to science remains low.

Conclusion

Good progress has been made on this chapter, and preparations are well advanced. Further efforts remain necessary, however, to ensure association and full participation of Croatia in the European Research Area.

4.26. Chapter 26: Education and Culture

Good progress has been achieved in the field of **education, training and youth**. The education reform process has continued under the Education System Development Plan for 2005–2010. Croatia is participating in the EU Education and Training 2010 Work Programme. Croatia performs very well in the EU benchmarks concerning early school leavers and upper secondary completion rates, but participation in pre-school education and adult participation in lifelong learning are very low. Additional efforts have been made in the development of a national qualifications framework (NQF). The Plan of Activities until 2012 has been adopted. Implementation of the Bologna process in higher education has continued. Future challenges include structural reform of universities and reforming the tuition fees, regulating the status and remit of the quality assurance agency, implementing a learning outcomes approach and improving recognition of prior learning. The Law on Quality Assurance in Higher Education has been adopted. The reform of vocational education and training has continued through adoption of the Law on Vocational Education and Training, which incorporates the principle of non-discrimination in access to education for EU citizens. Legislation implementing the Adult Education Act as well as a National Youth Programme 2009–2013 have also been adopted.

Good progress has been made in the preparations for the management of the Community Lifelong Learning and Youth in Action Programmes. The National Agency has started to implement preparatory measures, including staff training and launch of pilot projects. The respective Accession Partnership priorities in the field of education, training and youth have been partially met.

Good progress can also be reported in the field of **culture**. Efforts have continued to facilitate deeper participation in the Culture and Europe for Citizens Programmes.

Conclusion

Good progress has been made in the area of education, training, youth and culture. A good level of legal alignment has been achieved. Croatia should continue its efforts to prepare for the

management of Life Long Learning and Youth in Action programmes. Due attention also needs to be paid to adult education.

4.27. Chapter 27: Environment

Some progress has been made in the area of **horizontal legislation**. The transposition process is well advanced in this sector. However, the Directive on environmental liability is still not fully transposed or implemented. A Sustainable Development Strategy has been adopted. The Protocol on Strategic Environmental Assessment (SEA) to the Convention on Environmental Impact Assessment in a Transboundary Context (Espoo Convention) was ratified. Efforts to implement the SEA need to be stepped up. Implementation of provisions relating to public participation and access to justice in environmental matters remains weak. In this respect, cooperation with the judiciary should be strengthened.

Good progress has been achieved in the area of climate change. Implementing legislation on Kyoto flexible mechanisms has been enacted. The National Allocation Plan for greenhouse gas emissions allowances was adopted for the period 2010-2012. Preparations for connection to the EU Emissions Trading Scheme (EU ETS) are well advanced. The national GHG emission registry remains outstanding. Preparations in this area are proceeding well.

Croatia participates in the Community Civil Protection Mechanism.

There has been good progress in the field of **air quality**. The Directive on national emission ceilings for certain atmospheric pollutants is now fully transposed. Legislation on designation of zones and agglomerations according to categories of air quality was adopted. Establishment of the air quality monitoring and management system is entering its operational phase. The Plan for the Reduction of SO₂, NO_x and Dust Emissions from Large Combustion Plants and Gas Turbines has been adopted. Further, the National Plan for the Implementation of the Stockholm Convention on Persistent Organic Pollutants has been adopted. Although implementing legislation on limit values for emissions of pollutants into the air from stationary sources and on the quality of liquid fuels has been amended, an annual quantity of fuel that does not conform to prescribed quality standards is still placed on the market. The adjustment of petrol stations and terminals and modernisation of refineries is ongoing. Transposition of the new *acquis* related to ambient air quality and cleaner air for Europe is pending. Preparations in this area are progressing well.

Some progress has been made in the area of **waste management**. Implementing legislation relating to the management of waste from extractive industries and the management of polychlorinated biphenyls (PCB) and polychlorinated terphenyls (PCT) was adopted. Amending legislation on the classification of waste and on supervision of the transboundary movement of waste was also adopted. Sustained efforts in remediation of existing landfills and hot-spots and further establishment of systems for collection and management of different categories of waste are needed. Preparations in this area are progressing well.

There has been little progress in the **water sector**. The new Water Act and Act on Water Management Financing have not been enacted yet. This hampers the expected restructuring of the sector and continuation of the transposition process, which is slow at the moment.

Boundaries of river basins have been determined and implementing legislation relating to hazardous substances in waters and waste water has been enacted. Significant efforts have to be made to increase investments in this sector. Monitoring and reporting activities need to be improved. Significant efforts are still needed in this area.

There was some progress in the field of **nature protection**. Further efforts are needed to achieve full alignment with the *acquis*, in particular Directives 92/43/EC and 79/409/EEC. The Strategy and Action Plan for Conservation of Biological and Landscape Diversity were adopted and the Nature Protection Act was amended to ensure further alignment with the *acquis*. A draft list of proposed Natura 2000 sites has been discussed with relevant stakeholders. However, Croatia will need to step up efforts to finalise the list of Natura 2000 sites. Administrative capacity for the implementation and enforcement of the *acquis* needs further strengthening, especially within the State Institute for Nature Protection and at local level. In the area of nature protection Croatia is not yet sufficiently prepared.

There has been significant progress in the area of **industrial pollution control and risk management**. Implementing legislation relating to the integrated pollution prevention and control (IPPC) and the Seveso II Directives has been enacted. Registries of installations falling under the IPPC and the Seveso II Directives have been established. Efforts have been made in further developing the European Release and Transfer Register (EPRTR). Significant efforts will be required to ensure sufficient administrative capacity in this sector. Preparations in this area are proceeding well.

Good progress can be reported on **chemicals**. Implementing legislation on active substances in biocidal products and on safety data sheets has been enacted. Full transposition of the *acquis* in relation to the packaging and labelling of chemicals and the exports and imports of chemicals as well as biocides was achieved.

Some progress can be reported in the area of **genetically modified organisms (GMOs)**. Notification and the requirements for labelling and packaging of GMOs have been further regulated through implementing legislation. Further efforts will be required for achieving full alignment with the *acquis*. Laboratories and administrative capacity need to be further strengthened in order to implement and enforce the legislation. Preparations in GMOs are moderately advanced.

Good progress can be reported in the **noise** sector. Full transposition has been achieved with the adoption of the Noise Protection Act. Adoption of noise maps for towns and municipalities is progressing well. Preparations in this area are well on track.

In the **forestry** sector, activities related to the implementation of the existing Croatian legal framework have been continued.

Administrative capacity has overall further progressed across the sectors. However, the number of staff recruited is generally lower than what was planned in the action plan for setting up the necessary administrative capacities at national, regional and local level. Areas of concern include the nature protection and IPPC sectors. There is a clear need for institutional strengthening and capacity building at the local level. Given the high level of fragmentation of the environment sector across ministries and public bodies, improved coordination mechanisms and decision-making procedures are required.

Conclusion

There has been good progress in this chapter, especially in the areas of air quality, industrial pollution control and risk management, and climate change. Overall, Croatia's preparations are advancing well. However, considerable efforts are still needed in the water sector and nature protection, especially as regards implementation of the Water Framework Directive and the designation of Natura 2000 sites. Implementation of the horizontal *acquis*, not least strategic environmental assessment and access to justice in environmental matters, needs to be improved.

Administrative capacity needs further strengthening both at national and at local level.

4.28. Chapter 28: Consumer and Health Protection

There has been some progress in the field of **consumer protection**. As regards administrative capacity, two new officials have been hired in the Consumer Protection Department in the Ministry of the Economy, Labour and Entrepreneurship, bringing the total number of staff to 10. Government funding for regional counselling centres has continued, as well as activities for raising awareness on consumer protection. As for consumers' access to justice, the new Consumer Protection Act introduces the system of out-of-court settlement of consumer disputes. A special record of consumer disputes has been established, and training of judges is ongoing. However, administrative capacity needs to be further strengthened, especially as regards the State Inspectorate, the consumer movement needs to be further supported and consumers' access to justice further improved. Preparations in this field are advanced.

Good progress can be reported in the field of *product-safety related issues*. The General Product Safety Act has been amended, which is a key element for the accession negotiations in this chapter. A Regulation on a rapid information exchange system for products posing a risk to the health and safety of consumers has been adopted. However, it needs to be amended to bring it into line with the *acquis*. Also coordination between the RAPEX central contact point and local authorities as well as due enforcement of measures on general product safety need to be ensured. Preparations in this field are well advanced.

Good progress has been made in the area of *non-safety related issues*. The Consumer Protection Act has been amended, which is a key element for the accession negotiations in this chapter. It aims to ensure further alignment in many areas of the consumer protection *acquis*, among other things by establishing an appropriate enforcement mechanism against unfair terms in consumer contracts. An Act on Unpermitted Advertising has been adopted, aimed at aligning with the *acquis* on misleading/comparative advertising, as well as a Consumer Credit Act aiming at completing legal alignment in this area. Preparations in this field are reaching completion.

Good progress can be reported in the area of **public health**.

Substantial progress has been made in the area of *tobacco*. Legislation has been adopted completing legal alignment in the fields of tobacco advertising and tobacco products. This is a key element for the accession negotiations on this chapter. In this area, Croatia is in line with the *acquis*.

Some progress has been made in the field of *communicable diseases*. The Act on protection of the population against communicable diseases has been further amended and to a large extent brought into line with the *acquis* in this field as well as with the International Health Regulations. However, further legal adjustments are necessary in particular due to the current epidemiological situation concerning Influenza A(H1N1). Preparations in this field are well advanced.

Good progress can be reported in the area of *blood, tissues and cells*. Legislation has been adopted in the field of tissues and cells (including reproductive cells) aimed at completing legal alignment, inter alia with respect to reporting of serious adverse events and reactions for all non-reproductive tissues and cells. This is a key element for the accession negotiations on this chapter. As regards administrative capacity, a Department for the Inspection and Monitoring of Blood, Tissues and Cells has been established in the Ministry of Health and Social Welfare. However, quality management of all blood transfusion centres is not yet ensured, and facilities for handling tissues and cells have not yet been upgraded, restructured and licensed in accordance with the EU technical requirements. Preparations in this field are well under way.

No progress can be reported in the field of *mental health*. A Mental Health Promotion Strategy is being drafted. However, community-based services remain insufficiently developed as an alternative to institutionalisation, and financial resources allocated to mental health care are still scarce. The Accession Partnership priority in this field has therefore not been met. Preparations in this field are at an early stage.

Some progress has been made in the field of *drug* abuse prevention where an Action Plan to Combat Drug Abuse 2009–2012 has been adopted. Action Plans on *nutrition* and *alcohol* have been drawn up. In the area of *cancer screening*, preparations are under way for starting the National Programme for early detection of cervical cancer. Preparations in these areas are well on track.

Conclusion

There has been good progress in the area of consumer and health protection. Overall, a good level of legal alignment has been reached. Sustained efforts are necessary for further strengthening administrative capacity in order to implement and enforce legislation effectively in both areas. This is a key element for the accession negotiations on this chapter.

4.29. Chapter 29: Customs Union

Good progress has been made in the area of **customs legislation**. On 1 January 2009, the new Regulation on the customs tariff for 2009 entered into force, thereby aligning the Croatian tariff with the 2009 Combined Nomenclature. The Act amending the Act on the Customs Tariff abolished the remaining customs fees, which were due on the customs declaration, thus aligning with the EU legislation in the area. Some discrepancies with the *acquis* remain in allocation of quotas, duty relief, duty exemptions for passengers and the internal transit arrangements. Overall, alignment of the customs rules with the *acquis* is very high.

Good progress can also be reported on **administrative and operational capacity**. The Customs Administration has adopted and started to implement an Anti-corruption Programme. An anti-corruption awareness campaign has been launched within Customs and a policy of systematic rotation of staff developed. Work has continued on computerisation and interconnectivity. The Interoperability and Interconnectivity Strategy was updated in February 2009. The national domain of NCTS 3.2 has been completed and local testing performed successfully. Development of the NCTS Trader Module, Export Control System (ECS), and ITMS sub-systems started at the end of 2008. The Croatian customs administration still has very limited in-house capacity to guarantee the continuity of its IT services and remains heavily dependent on external companies. Overall, in the area of administrative and operational capacity, Croatia has consistently addressed its targets and priorities.

Conclusion

Good progress has been made overall. Croatian customs legislation is well aligned with the *acquis* and additional alignment was achieved during the period. Croatia has also continued to make progress on its administrative capacity, and started to implement a coherent anti-corruption policy within Customs. Progress has also continued in the area of IT interconnectivity, where implementation of the IT strategy has continued steadily. Efforts need to continue in the remaining areas of legislative alignment, in implementing the Anti-Corruption Strategy and in IT interconnectivity.

4.30. Chapter 30: External Relations

There has been good progress in the field of the **common commercial policy**. Croatia continued to cooperate and coordinate closely with the Commission and to align with the policies and positions of the EU towards third countries and within international organisations, particularly the World Trade Organisation.

In June 2009, Croatia imposed an erga-omnes provisional safeguard measure on semi-hard cheese and cheese supplements in breach of the WTO rules. Measures were imposed two months before the initiation of an investigation and no evidence showing that the conditions required for the imposition of measures has been provided. Thus these legally unwarranted measures have already negatively affected the EU exports and Croatia needs to address this issue as a matter of urgency.

In relation to dual-use goods, Croatia continued to align with the revised list of dual-use items and technology. Croatia simplified the procedure for issuance of export and import permits for dual-use goods, strengthened provisions on the fight against illicit exports and started various training activities in order to enhance administrative capacity. It needs to continue to work on the remaining adjustments and on further enhancing its administrative, control and reporting capacity for dual-use goods, in particular, on the training of customs officers. Overall, preparations in the area of the common commercial policy are well on track.

In the area of bilateral trade and investment **agreements with third countries**, Croatia actively participates in the work of the Central European Free Trade Agreement (CEFTA). Croatia continued implementing its action plan by bringing international agreements into line with the *acquis*. Croatia needs to continue implementing the Action Plan, as adopted. Preparations in this area are well advanced.

Some progress can be reported on **development policy and humanitarian aid**. A National Strategy for Development Cooperation for the period 2009-2014 has been adopted. The department responsible its implementation is now operational. Croatia will need to complete the required legal framework in this area. Generally, preparations in this area are well advanced. Following the adoption of laws for development policy and humanitarian aid, greater financial and human resources are required to ensure their progression.

Conclusion

Croatia has made some progress in this chapter. Provided Croatia continues preparations as scheduled and improves its administrative capacity, it should be able to apply the *acquis* and participate in the common commercial policy upon accession. However, Croatia needs to respect its international obligations when resorting to trade defence measures. Efforts are still needed with regard to development policy and humanitarian aid.

4.31. Chapter 31: Foreign, Security and Defence Policy

The regular **political dialogue** between the EU and Croatia has continued to cover foreign policy issues. (*Concerning neighbourly relations with other enlargement countries and Member States, see section 2.3 under Political criteria.*)

As regards the **common foreign and security policy (CFSP)**, Croatia has continued to systematically align itself with all relevant EU common positions, declarations and statements. Croatia has continued to develop its administrative capacity to work within the EU CFSP structures.

The post of Political Director in the Ministry for Foreign Affairs and European Integration remains to be formally established.

A new Act on international *restrictive measures* aimed at comprehensive and more efficient application of sanctions regimes was passed in November 2008. Inter-agency coordination has improved.

As regards *non-proliferation*, the Government of Croatia adopted in September 2009 a National Strategy and Action Plan for the Control of Small Arms and Light Weapons. Public awareness activities have continued, including measures to collect and destroy weapons. Croatia signed and ratified the Convention on Cluster Munitions. However, while the legislative framework for arms control is satisfactory, there remains a need to further strengthen implementation and enforcement capacity as well as transparency of arms-related information.

With regard to *cooperation with international organisations*, Croatia has, as a member of the UN, the OSCE and the Council of Europe, been fully involved in the policy-making of these organisations. In 2009, Croatia began the second year of its mandate as a non-permanent member of the Security Council. Croatia became a member of NATO in April 2009. As regards the International Criminal Court, see *Political criteria — Regional issues and international obligations*.

There have been no particular developments with regard to *security measures (classified information)*.

Croatia has remained committed to the development of the European security and defence policy (ESDP). Administrative capacity-building measures have continued, including training and greater participation of Croatian officials in various fora with EU counterparts. Croatia further reinforced its participation in EU missions. Croatia joined the EU's military operation in Chad and the Central African Republic (EUFOR TCHAD/RCA) with a 15-member reconnaissance team. In April 2009 the Croatian Parliament adopted a decision on the participation of five members of Croatia's armed forces in the EU operation off the Somali coast (EU NAVFOR Somalia – ATALANTA). Croatia continued to provide logistical (host nation) support to the EUFOR Althea mission in Bosnia and Herzegovina.

Croatia continued to support EU civilian missions. Croatia participates in the EU Rule of Law Mission in Kosovo (EULEX Kosovo) and the EUPOL Mission in Afghanistan with four police officers in total. Croatia has continued to take part in international peacekeeping efforts with, as of September 2009, 145 members of the armed forces and 9 police officers taking part in 10 UN missions.

Conclusion

Croatia has made good progress in this chapter. Overall, Croatia has reached a good level of alignment in the area of foreign, security and defence policy. Croatia continues to participate in several EU ESDP missions. In order to be fully prepared for accession, Croatia needs to strengthen implementation and enforcement of arms control including transparency of arms-related information, and to further improve capacity for full implementation of CFSP-ESDP.

4.32. Chapter 32: Financial Control

Progress can be reported in the area of **public internal financial control (PIFC)**. The revised Internal Audit Manual was adopted in November 2008. The new Budget Law, removing

inconsistency with the provisions of the PIFC Law, entered into force on 1 January 2009. A new PIFC Development Strategy for the period 2009-2011 was adopted by the Government in September.

With regard to the institutional framework, the Central Harmonisation Unit (CHU) was reorganised in February 2009. However, strengthening of training facilities needs to be continued by gradually shifting the CHU's focus from training towards coaching and monitoring activities. Also, the strengthening of overall capacity of all budget users at central and local levels needs to be continued, including through development of a risk management approach. The focus of audit work has been on auditing EU funds, with limited resources available for the audit of national funds. The internal audit profession needs further strengthening, including increased focus on system-based and performance audits.

In the area of external audit no progress can be mentioned concerning the consolidation of the State Audit Office's (SAO) functional and financial independence in the Constitution. The implementation of the SAO's Strategic Development Plan for the period 2008-2012 is ongoing. Continued efforts are required to train auditors in modern audit techniques, especially on performance audit and audit of EU funds, and moving towards a systems-based audit approach. The annual procedure for reporting to Parliament needs reconsideration to allow the SAO's annual report to contribute to the budget discharge procedure.

Progress has been made on the protection of the EU's financial interests. As per the new rules of procedure of the Ministry of Finance, the Department for Combating Irregularities and Fraud (AFCOS) was established as an independent department under the direct supervision of the Minister of Finance. As the central contact unit of the AFCOS network, the department is expected to have sufficient capacity in the field of fraud prevention, detection and follow-up to act as the unit coordinating with OLAF. The drafting of the Anti-fraud Strategy and Action Plan is well under way and a consultation process was launched in June 2009. There has been improvement in the reporting of irregularities. The Croatian authorities have achieved more effective compliance with the reporting requirements. However, follow-up (especially with regard to recoveries) needs to be further enhanced.

Progress has been made in harmonising the Criminal Code with PIF instruments, as the Act amending the Criminal Code entered into force as from January 2009. Some further clarifications are required to remove ambiguities from the Croatian Criminal Code and to establish its precedence in matters relating to protection of the EU's financial interests.

Some progress can be reported on **protection of the euro against counterfeiting**. The National Counterfeit Centre (NCC), the National Analysis Centre (NAC) and the Coin National Analysis Centre (CNAC) within the Croatian National Bank became operational as from March 2009. The National Central Office (NCO) has been established in accordance with the requirements of the International Convention for the Suppression of Counterfeiting Currency.

Conclusion

Croatia has made progress under this chapter. Continued efforts are needed to ensure sustainable development of the overall PIFC system at both central and local government level. The functional and financial independence of the SAO needs to be anchored in the Constitution.

4.33. Chapter 33: Financial and Budgetary Provisions

There has been good progress in this chapter. The unit for the coordination and management of the

own resources system in the Ministry of Finance has continued to develop its capacity to play the coordination role required of it from accession. The capacity of the relevant institutions responsible for the system of own resources has improved. An action plan for the implementation of the system of administration of the EU's own resources has been adopted and implementation is under way.

As regards traditional own resources (TOR), Croatia is in the process of upgrading its existing information and accounting systems and simulations of the 'A' and 'B' accounts have been carried out. However, Croatia needs to speed up the development of the TOR IT application for establishing customs duties in the A and B accounts and the automatic production of A and B account statements used to make duties available to the EU budget. Also, Croatia has to further strengthen the independent internal control and external audit of the collection and accounting of TOR. Post-clearance control at traders' premises should be further strengthened. Croatia still needs to put in place a system for sugar levies and a write-off system for irrecoverable debts in line with the EU rules. The competent departments for OWNRES reporting need to be designated and their working procedures established.

In the area of VAT-based own resources, a simulation of the VAT base was carried out, covering the collection of revenue, compensation calculations and the analysis and processing of data necessary for the calculation of the Weighted Average Rate (WAR). While the basic principles are well understood, more detailed statistical data will still be required for the WAR calculation and capacity building should continue.

As regards the GNI-based resource, application of the ESA95 methodology and definitions has improved significantly. Continued efforts will, however, be needed to further improve the quality and exhaustiveness of the national accounts and GNI calculations.

Croatia needs to continue its efforts in underlying policy areas linked to the application of the own resources system, in particular customs, taxation, statistics and financial control. This includes setting up effective instruments to combat customs duty and VAT fraud so that the financial interests of the EU can be protected.

Conclusion

There has been good progress in this chapter, notably the further development of institutional capacity for applying own resources rules. Overall, Croatia has reached a good level of alignment with and capacity to implement the *acquis*, except for sugar levies. Croatia should now continue to implement its action plan, further develop administrative capacity and put in place rules and procedures.

STATISTICAL ANNEX

STATISTICAL DATA (as of 14 September 2009) Croatia

Basic data

	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Population (thousand)		4 527e	4 498e	4 439b	4 445	4 443	4 442	4 444	4 443	4 441	4 436
Total area of the country (km ²)	1)	56 542	56 542	56 542	56 542	56 594b	56 594	56 594	56 594	56 594	56 594

National accounts

	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Gross domestic product (GDP) (million national currency)	2)	164 054	176 690	190 796	208 223	227 012	245 550	264 367	286 341	314 223	342 159
GDP (million euro)	2)	21 638	23 146	25 538	28 112	30 011	32 759	35 725	39 102	42 833	47 370
GDP (euro per capita)		4 751	5 229	5 752	6 331	6 759	7 380	8 043	8 807	9 656	10 678
GDP (in Purchasing Power Standards (PPS) per capita)		8 800.0e	9 400.0e	9 900.0e	10 700e	11 200e	12 100	12 700	13 800	15 200	15 800
SI: GDP (in PPS per capita, EU-27=100)		49.5e	49.2e	50.3e	52.3e	54.3e	55.8	56.6	58.4	61.1	63.0
SI: Growth rate of GDP (national currency, at constant prices, % change on previous year)		-1.5	3.0	3.8	5.4	5.0	4.3	4.2	4.7	5.5	2.4
SI: Employment growth (national accounts, % change on previous year)		-3.3	4.0	-5.4	4.2	0.6	1.7	0.8f	-0.6f	3.5f	1.1f
Labour productivity growth: GDP growth per person employed (% change on previous year)		1.9	-0.9	9.8	1.2	4.3	2.5	3.4e	5.4e	1.9e	1.3e
SI: Unit labour cost growth (national accounts, % change on previous year)		4.8	-3.4	-4.2	1.3	-7.3	6.7	-0.4e	-10.2e	-0.7e	1.4e
SI: Labour productivity (GDP in PPS per person employed, EU-27=100)		63.3e	61.3e	66.5e	66.6e	68.6e	69.5	70.4e	73.8e	75.7e	76.6e
Gross value added by main sectors (%)											
Agriculture	2)	9.1	8.4	8.4	8.2	6.8	7.2	6.5	6.3	6.1	6.4
Industry	2)	23.1	23.4	22.8	21.9	21.4	21.8	20.9	20.6	20.4	20.2
Construction	2)	5.3	4.9	5.4	5.5	6.6	7.1	7.4	7.7	7.7	8.3
Services	2)	62.5	63.2	63.4	64.4	65.3	63.9	65.2	65.3	65.8	65.0
Final consumption expenditure, as a share of GDP (%)	3)	85.5	84.6	82.7	83.1	81.4	80.4	80.2	78.9	78.7	77.7
Gross fixed capital formation, as a share of GDP (%)	2)	20.1	18.8	19.4	21.2	25.0	24.6	24.6	26.1	26.2	27.6
Changes in inventories, as a share of GDP (%)	2)	0.6	-0.2	1.7	4.0	1.5	1.3	1.7	2.0	2.7	3.2
Exports of goods and services, relative to GDP (%)	2)	36.5	42.0	43.8	41.0	42.9	43.3	42.6	43.4	42.8	41.9
Imports of goods and services, relative to GDP (%)	2)	42.7	45.3	47.6	49.4	50.8	49.6	49.1	50.4	50.4	50.3

Industry

	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Industrial production volume index (2000=100)	4)	98.3	100.0	106.0	111.8	116.3	120.6	126.7	132.4	139.8	142.1

Inflation rate

	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
SI: Consumer price index (CPI), (total, % change on previous year)		4.0	4.6	3.8	1.7	1.8	2.1	3.3	3.2	2.9	6.1

Balance of payments

	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Balance of payments: current account total (million euro)		-1 429	-568	-821	-2 099	-1 889	-1 434	-1 976	-2 715	-3 237	-4 438
Balance of payments current account: trade balance (million euro)		-3 102	-3 492	-4 595	-5 958	-6 971	-6 724	-7 518	-8 344	-9 434	-10 866

Balance of payments current account: net services (million euro)		1 545	2 470	3 303	3 285	4 933	4 769	5 318	5 705	6 266	6 969
Balance of payments current account: net income (million euro)		-465	-505	-628	-578	-1 095	-670	-959	-1 183	-1 112	-1 576
Balance of payments current account: net current transfers (million euro)		594	959	1 099	1 152	1 245	1 192	1 184	1 107	1 043	1 035
of which government transfers (million euro)		-123	25	65	32	71	3	10	-9	-17	-56
Net foreign direct investment (FDI) (million euro)		1 304	1 136	1 258	531	1 657	671	1 276	2 557	3 483	3 203
Foreign direct investment (FDI) abroad (million euro)		-58	-5	-210	-607	-106	-279	-192	-208	-184	-128
of which FDI of the reporting economy in EU-27 countries (million euro)		-21	15	-152	-72	-7	-14	-66	37	-563	93
Foreign direct investment (FDI) in the reporting economy (million euro)		1 363	1 141	1 467	1 138	1 762	950	1 468	2 765	3 667	3 330
of which FDI of EU-27 countries in the reporting economy (million euro)		1 186	916	1 344	1 063	1 498	919	1 439	3 500	3 702	3 144

Public finance	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
General government deficit/surplus, relative to GDP (%)	5)	:	:	-5.6	-3.6	-4.8	-3.8	-3.5	-3.0	-2.5	-1.4
SI: General government debt, relative to GDP (%)		:	:	34.8	34.8	35.9	37.8	38.3	35.7	33.1	33.5

Financial indicators	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Gross foreign debt of the whole economy, relative to GDP (%)		47.0	53.0	53.3	53.9	66.3	70.0	72.1	74.9	76.9	82.6
Gross foreign debt of the whole economy, relative to total exports (%)		133.0	130.2	125.9	136.1	151.3	161.0	168.6	172.3	179.8	197.3
Money supply: M1 (banknotes, coins, overnight deposits, million euro)		1 805	2 373	3 216	4 148	4 432	4 505	5 263	6 606	7 901	7 539
Money supply: M2 (M1 plus deposits with maturity up to two years, million euro)		:	:	:	:	:	:	:	:	:	:
Money supply: M3 (M2 plus marketable instruments, million euro)		:	:	:	:	:	:	:	:	:	:
Total credit by monetary financial institutions to residents (consolidated) (million euro)		8 587	9 483	11 891	15 119	16 526	18 417	22 836	27 274	30 863	34 756
Interest rates: day-to-day money rate, per annum (%)		9.3	6.9	3.0	1.3	4.3	5.9	3.4	2.4	5.6	6.6
Lending interest rate (one year), per annum (%)		20.9	20.6	19.5	16.5	15.0	14.4	13.1	12.1	12.1	12.2
Deposit interest rate (one year), per annum (%)		9.5	8.2	6.6	5.4	3.8	3.8	3.9	4.0	4.2	4.8
euro exchange rates: average of period - 1 euro = ... national currency		7.582	7.634	7.471	7.471	7.564	7.496	7.400	7.323	7.336	7.223
Effective exchange rate index (2000=100)		95.4	100.0	98.7	96.5	93.7	90.4	:	:	:	:
Value of reserve assets (including gold) (million euro)		3 013	3 783	5 334	5 651	6 554	6 436	7 438	8 725	9 307	9 121

External trade	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Value of imports: all goods, all partners (million euro)		:	:	:	11 327	12 510	13 354	14 950	17 105	18 686	20 762
Value of exports: all goods, all partners (million euro)		:	:	:	5 188	5 439	6 454	7 069	8 252	8 855	9 342
Trade balance: all goods, all partners (million euro)		:	:	:	-6 139	-7 071	-6 901	-7 880	-8 853	-9 832	-11 420
Terms of trade (export price index / import price index)	6)	:	98.3	94.4	97.8	97.5	109.3b	92.6	100.2	97.5	96.1
Share of exports to EU-27 countries in value of total exports (%)		:	:	:	66.1	68.3	65.8	63.3	64.3	60.9	62.1
Share of imports from EU-27 countries in value of total imports (%)		:	:	:	71.9	73.3	71.0	67.9	67.2	64.8	64.2

Demography	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Natural growth rate: natural change (births minus deaths) (per 1000 inhabitants)		-1.5	-1.5	-1.9	-2.4	-2.9	-2.1	-2.1	-2.0	-2.4	-2.3e
Infant mortality rate: deaths of children under one year of age per 1000 live births		7.7	7.4	7.7	7.0	6.3	6.1	5.7	5.2	5.6	4.5

Life expectancy at birth: male (years)		:	70.5	71.1	71.2	71.4	72.0	71.8	72.5	72.3	72.4
Life expectancy at birth: female (years)		:	77.8	78.1	78.3	78.4	79.0	78.8	79.3	79.2	79.6

Labour market	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Economic activity rate (15-64): share of population aged 15-64 that is economically active (%)	7)	62.6	62.2	62.2	62.9	62.4	63.7	63.3	62.6	63.2	63.2
SI: Employment rate (15-64): share of population aged 15-64 that is in employment (%)	7)	53.2	51.3	51.8	53.4	53.4	54.7	55.0	55.6	57.1	57.8
Share of male population aged 15-64 that is in employment (%)	7)	59.0	57.4	59.0	60.5	60.3	61.8	61.7	62.0	64.4	65.0
Share of female population aged 15-64 that is in employment (%)	7)	47.8	45.5	44.9	46.7	46.7	47.8	48.6	49.4	50.0	50.7
SI: Employment rate of older workers (55-64): share of population aged 55-64 that is in employment (%)	7)	25.9	24.2	23.7	24.8	28.4	30.1	32.6	34.3	35.8	36.7
Employment by main sectors (%)											
Agriculture	7)	16.7	11.7	15.6	15.5	16.9	17.0	17.3	14.2	13.0	13.6
Industry	7)	23.9	22.7	23.1	22.6	22.1	21.4	20.5	20.9	21.8	21.6
Construction	7)	6.6	5.9	6.3	7.2	8.1	8.2	8.2	8.4	8.8	8.9
Services	7)	52.8	59.6	55.0	54.6	52.8	53.2	54.0	56.3	56.4	55.9
SI: Unemployment rate: share of labour force that is unemployed (%)	7)	14.5	17.0	16.3	14.7	14.1	13.6	12.6	11.1	9.6	8.4
Share of male labour force that is unemployed (%)	7)	13.5	15.9	14.4	13.2	12.8	12.0	11.6	9.8	8.4	7.0
Share of female labour force that is unemployed (%)	7)	15.7	18.2	18.7	16.5	15.6	15.6	13.8	12.7	11.2	10.1
Unemployment rate of persons < 25 years: share of labour force aged <25 that is unemployed (%)	8)	39.2	43.1	41.7	34.4	35.8	33.8	32.0	28.8	24.0	22.0
SI: Long-term unemployment rate: share of labour force that is long-term unemployed (%)	9)	7.3	9.1	10.1	8.9	8.4	7.3	7.4	6.7	5.9	5.3

Social cohesion	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Average nominal monthly wages and salaries (national currency)	10)	4 551.0	4 869.0	5 061.0	5 366.0	5 623.0	5 985.0	6 248.0	6 634.0	7 047.0	7 544.0
Index of real wages and salaries (index of nominal wages and salaries divided by the CPI) (2000=100)	10)	98.4	100.0	99.2	103.2	106.1	112.2	113.4	116.6	120.4	121.5
SI: Early school-leavers: share of population aged 18-24 having not completed upper secondary education and not currently in education or training (%)	8)	:	:	:	8.3	8.4	6.2	4.8	5.1	3.9	3.7

Standard of living	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Number of passenger cars per 1000 population		234.9	250.1	269.3	280.0	291.1	301.1	311.6	323.2	335.7	348.2
Number of subscriptions to cellular mobile telephone services per 1000 population	11)	79.7	247.2b	390.0	520.4	571.0	638.3	821.4	989.2	1 133.7	1 325.4

Infrastructure	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Density of railway network (lines in operation, per 1000 km ²)		47.8	47.8	47.8	47.8	47.7	47.7	47.7	47.7	47.7	47.7
Length of motorways (thousand km)		0.4	0.4	0.4	0.5	0.6	0.7	0.8	0.9	1.0	1.0

Innovation and research	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
SI: Spending on human resources (public expenditure on education) relative to GDP (%)		4.2	4.5	4.2	4.3	4.5	:	:	:	:	:
SI: Gross domestic expenditure on research & development, relative to GDP (%)		1.0	1.1	0.9	1.0	1.0	1.1	0.9	0.8	0.8	:
SI: Percentage of households who have Internet access at home (%)		:	:	:	:	:	:	:	:	41.0	45.0

Environment	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
SI: Total greenhouse gases emissions, CO2 equivalent (tons, 1990=100)		83.2	82.7	86.6	89.7	95.4	95.1	97	98.1	103.2	:

SI: Energy intensity of the economy (kg of oil equivalent per 1000 euro GDP 2004)		299.9	286.0	280.3	288.1	281.0	269.9	260.8	250.4	247.3	:
SI: Share of renewable energy in electricity consumption (%)		45.1	40.0	42.7	33.9	29.4	41.0	58.1	60.5	47.0	:
SI: Road freight transport as a share of total inland freight transport (modal split of freight transport) (%)		:	:	75.9	76.4	76.2	76.6	76.0	74.8	74.0	76.0

Energy	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Primary production of all energy products (thousand TOE)		3 570	3 562	3 730	3 689	3 727	3 852	3 781	4 128	4 037	:
Primary production of crude oil (thousand TOE)		1 394	1 328	1 232	1 200	1 138	1 079	1 017	985	937	:
Primary production of hard coal and lignite (thousand TOE)		9	0	0	0	0	0	0	0	0	:
Primary production of natural gas (thousand TOE)		1 267	1 355	1 642	1 732	1 789	1 796	1 854	2 204	2 349	:
Net imports of all energy products (thousand TOE)		4 427	4 174	4 166	4 967	4 985	5 090	5 234	4 866	5 315	:
Gross inland energy consumption (thousand TOE)		7 959	7 819	7 959	8 624	8 828	8 842	8 902	8 948	9 323	:
Electricity generation (thousand GWh)		12.2	10.7	12.2	12.3	12.7	13.3	13.1	13.0	12.4	:

Agriculture	Note	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Agricultural production volume index of goods and services (producer prices, previous year=100)		98.8	88.7	108.5	107.7	84.1	111.9	91.3	104.4	96.0	:
Total utilised agricultural area (thousand hectare)		2 032	1 169b	1 178	1 181	1 196	1 176	1 211	1 230	1 202	1 288
Livestock: cattle (thousand heads, end of period)		438	427	438	417	444	466	471	483	467	454
Livestock: pigs (thousand heads, end of period)		1 362	1 234	1 234	1 286	1 347	1 489	1 205	1 488	1 348	1 104
Livestock: sheep and goats (thousand heads, end of period)		567	608	632	677	673	848	931	783	738	727
Production and utilisation of milk on the farm (total whole milk, thousand tonnes)		641	626	674	716	686	708	813	870	883	828p
Crop production: cereals (including rice) (thousand tonnes, harvested production)		2 881	2 312	2 829	3 080	2 014	3 067	3 039	3 034	2 534	3 724p
Crop production: sugar beet (thousand tonnes, harvested production)		1 114	482	965	1 183	678	1 260	1 338	1 560	1 583	1 270p
Crop production: vegetables (thousand tonnes, harvested production)		537	196	208	218	154	150	286	304	281	279p

SI = Structural Indicator

: = not available

e = estimate

f = forecast

p = provisional

b = break in series

- 1) Land area, break in series in 2003 due to improved methodology.
- 2) For 2005-2007, data is based on quarterly values.
- 3) For 2005-2007, NPISH is not included.
- 4) Gross series; include NACE sections C to E.
- 5) Privatisation revenues are excluded and reclassified to the financing of the balance.
- 6) Calculated on the basis of export and import values expressed in US dollars; break in series in 2004: change in methodology as of 1 January 2004.
- 7) For 1998-2001, data refer to the second half of the year; in 2007, data refer to the annual average of quarterly data.
- 8) For 1998-2006, data refer to the second half of the year; in 2007, data refer to the annual average of quarterly data.
- 9) For 1998-2001, data refer to the second half of the year and long-term unemployment refers to thirteen months or more; in 2007, data refer to the third quarter.
- 10) From 2004 onwards the number of persons employed in the police and defense-related activities are included.
- 11) Number of subscriptions to cellular mobile telephone services is presented as total sum of GSM and UMTS; break in series: from 2000 onwards data present the number of prepaid and postpaid users.