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Montenegro 2006 Progress Report

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Montenegro 2006 Progress Report

1. INTRODUCTION

1.1. Preface

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

This is the first progress report for Montenegro since its independence following a referendum which was held on 21 May 2006. The report:

- briefly describes the relations between Montenegro and the Union;
- analyses the political situation in Montenegro in terms of democracy, the rule of law, human rights, protection of minorities, and regional issues;
- analyses the economic situation in Montenegro;
- reviews Montenegro's capacity to implement European standards, that is, to gradually approximate its legislation and policies with those of the *acquis*, in line with a Stabilisation and Association Agreement and the European Partnership priorities.

The period covered by this report is 1 October 2005 to 30 September 2006. 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 await 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 Montenegro, the Member States, European Parliament reports¹ and information from various international and non-governmental organisations.

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

1.2. Relations between the EU and Montenegro

Montenegro proclaimed its independence on 3 June 2006, following a referendum held on 21 May 2006. On 12 June 2006, the EU decided to establish relations with Montenegro as a sovereign and independent state. All EU Member States recognised the independence of Montenegro and established diplomatic relations with it.

¹ The *rapporteur* for Montenegro is Mr Vernola.

² Enlargement Strategy and Main Challenges 2006 – 2007.

Currently there is no contractual framework between the European Union and Montenegro. Contractual relations between the EU and Montenegro are to be established through the conclusion of a Stabilisation and Association Agreement (SAA). In the meantime Montenegro continues to benefit from the Autonomous Trade Measures granted by the EU.

From 10 October 2005 the Commission had been conducting negotiations for the conclusion of an SAA with the State Union of Serbia and Montenegro. The negotiations were based on the "twin-track" approach, which implies distinct negotiations with the two Republics on trade, economic and other relevant sectoral policies. Negotiations on the Stabilisation and Association Agreement had been progressing well and substantial progress had been made. Following the 21 May referendum and the independence of Montenegro, the Council adopted a new negotiating mandate for Montenegro in July 2006. These negotiations for an SAA with Montenegro were then launched on 26 September 2006. Negotiations will build upon results achieved in the framework of the SAA negotiations with the former State Union. A key challenge for Montenegro in the context of the SAA will be to upgrade its administrative capacity so that it is in a position to implement the provisions of the agreement.

The Commission has continued to closely monitor progress made by Serbia and Montenegro, notably in the context of the Enhanced Permanent Dialogue. The Enhanced Permanent Dialogue has continued with Montenegro separately after the independence of Montenegro, and a meeting took place in July 2006. In September 2006 the Council decided to launch political dialogue with Montenegro.

A revised European Partnership for Serbia and Montenegro was adopted by the Council in January 2006. In March 2006 Montenegro adopted an Action Plan addressing the priorities of the European Partnership relating to Montenegro.

The Commission made a proposal to the Council in July 2006 requesting a mandate to negotiate visa facilitation and readmission agreements with Montenegro.

Montenegro has continued to receive EC pre-accession **financial assistance**. In 2006, €23 million were allocated to Montenegro.

2. POLITICAL CRITERIA

This section examines progress made by Montenegro 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, and the respect for international obligations, such as cooperation with the UN International Criminal Tribunal for the former Yugoslavia.

2.1. Democracy and the rule of law

Constitution

Montenegro proclaimed its independence on 3 June 2006, following a **referendum** held on 21 May 2006. This referendum was held in line with the Constitutional Charter of the State Union of Serbia and Montenegro. A special referendum law was adopted on 1 March 2006. In this referendum, 55.5% supported independence and 44.5% voted against. This result exceeded the 55% threshold needed to validate a positive result under modalities decided by

political consensus in Montenegro in line with the recommendations of the European Union. The referendum was conducted in line with international standards.

Following the official announcement of the final referendum results, the Montenegrin Parliament adopted a Declaration of Independence on 3 June 2006, which marked the end of the former State Union. The Serbian Parliament adopted a decision which confirmed the status of Serbia as a successor state to the State Union, in accordance with the Constitutional Charter. The resolution of pending issues with Serbia has been proceeding smoothly. The remaining issues concern citizenship rights and social security in particular.

Montenegro then began the process of seeking international recognition as well as a seat at international organisations. On 12 June 2006, the EU decided to establish relations with Montenegro as a sovereign and independent state. All EU Member States recognised the independence of Montenegro and diplomatic relations were established. Montenegro applied for membership in the Council of Europe on 6 June 2006. Pending the outcome of the accession procedure, Montenegro continues to participate in the work of the Council of Europe under the status of observer or ad hoc participant. On 21 June 2006, Montenegro was admitted to the OSCE and on 28 June 2006 it became the 192nd member state of the United Nations. Montenegro has so far been recognised by 83 states.

The Proclamation of Independence of Montenegro on 3 June 2006 provided for a transitional implementation of the legislation of the former State Union, including international obligations, until the adoption of relevant Montenegrin legislation. However, the formula adopted specifies that such legislation is valid provided it is not "in collision with the legal order and interests" of Montenegro. This formulation raises concerns over legal certainty in Montenegro, as it does not provide an unequivocal response to the question on the applicable legislation in the country. Montenegro should therefore clarify which laws and international obligations of the State Union continue to apply after independence.

Montenegro is gradually upgrading its capacity to perform its new competences, notably in the areas of defence, foreign affairs, visa, asylum and migration, intellectual property and standardisation. Particular attention should be paid to the signature and ratification of international instruments, given that Montenegro is not the successor of the Union and, therefore, needs to fulfil the necessary steps to adopt the relevant treaties and conventions.

The formerly common defence structures of the State Union have been divided between the two Republics. The large majority of requests by military personnel to be transferred from Montenegro to Serbia have been accepted. Property issues have been resolved according to the territorial principle. Montenegro adopted a National Security Strategy in June 2006. This reflects Montenegro's commitment to become part of regional and global security systems and to introduce professionalisation of the army, transparency and civilian control.

Following independence Montenegro launched preparations for the adoption of a new Constitution. The Constitution needs to be developed and adopted in line with European values, standards and practices, especially in the area of human and minority rights. It also needs to guarantee the independence and the efficiency of the judicial system and assist the European integration process of Montenegro.

Parliament

The activities of the Parliament focused on the legislative preparation and organisation of the referendum. However, the referendum outcome raised new political and party disputes. The

opposition parties which had supported the preservation of the State Union abstained from all actions leading to independence.

The Parliament has continued its legislative activities and adopted 42 legal acts, in addition to the Decision and the Declaration on Independence.

The Committee for European Integration has continued to be affected by insufficient resources and expertise, including the lack of specialised staff. No compatibility checks of new legislation with the *acquis* have been performed at the level of Parliament.

The Parliament adopted new Rules of Procedure in July, prepared with the cooperation of the ruling majority and the opposition parties. It was adopted by a broad consensus.

Parliamentary elections took place (in parallel to municipal elections) on 10 September 2006. According to the International Election Observation Mission led by OSCE-ODIHR, these were held largely in line with international and European standards. However, a number of challenges were identified, related mainly to media behaviour and the selection of MPs. These remaining challenges need to be addressed. Voter turnout was relatively high at 71,37%. According to the official results, the Coalition for European Montenegro of outgoing Prime Minister Milo Djukanovic won 47,65% of the votes and the absolute majority of seats in the Parliament (41). 3 Parties and coalitions have shared the biggest share of the remaining votes, below 15% each, whereas a number of smaller parties have won between 1 and 3 seats.

The parliament resulting from the parliamentary elections of 10 September 2006 is considered a constitutive assembly by law. The number of Parliament seats has been increased from 75 to 81.

A number of issues related to the work of the Parliament require attention. The lack of consensus on major issues between government and opposition continues to seriously affect the efficiency of the parliament. A lack of consensus persisted in cases involving sensitive texts, such as the new Law on Minority Rights and Freedoms. This was only adopted on the eve of the referendum after two years of discussion. This has affected the overall political framework relevant for its implementation. Insufficient administrative resources have also affected Parliament's work.

Following independence, the Parliament will have to upgrade its capacities in the areas of legislation and governmental control, in particular regarding the new competences exercised by state institutions. Montenegro will have to make a particular effort to make sure that Parliament oversees defence and security structures satisfactorily, given that civilian oversight of the military in the former State Union was insufficient and often criticised by many observers.

The implementation of the new rules of procedure, which assist the role of the opposition and streamline parliamentary work, need to be coupled with an upgrading of the resources for the parliament. The process of transposition of the *acquis* needs to be enhanced and the role of the Committee for European Integration strengthened.

Government

The activities of the Montenegrin government were largely affected by the referendum process. Apart from adopting several declarations on its post-referendum commitments, the Government approved a comprehensive Action Plan in April 2006 related to priority legal and

institutional measures necessary for Montenegro to function as an independent state. It also focused on reforms recommended by the European partnership as well as on the process of negotiations for an SAA.

The Ministry for International Economic Relations and European Integration has played an essential role in mobilising government resources for the implementation of the European Partnership and has been efficient in the coordination of European integration process, including the conduct of Stabilisation and Association Agreement negotiations. Specific coordination frameworks have been set up with regard to the programming and implementation of the Instrument for Pre-Accession (IPA) programme and the SAA negotiations. However, overall strategic planning and coordination are weak. For example, inter-ministerial consultations are not required before discussions take place at the level of government commissions. The efficiency of the decision-making system also needs to be enhanced. The government also needs to further upgrade capacities in ministries and relevant agencies in order to successfully deal with the tasks related to European integration, such as impact assessments and compatibility checks of draft legislation against the *acquis*.

Public administration

Progress in establishing the legislative framework for public administration reform has continued. Reform monitoring mechanisms have been set up. A new recruitment system is in place but it has not been fully implemented. Implementing regulations have been prepared by the Authority for Human Resources Management. The staffing situation of the Authority has been improved and a separate budget has been allocated. Comprehensive training of civil servants is ongoing. Mandatory allocations for training are being introduced. A Code of Ethics for Civil Servants and Public Employees was adopted in December 2005 and distributed to all state employees. The authorities have taken some steps to improve implementation capacities. However, the public administration continues to suffer from serious weaknesses in terms of available resources, accountability and implementation capacity. There are serious shortcomings in monitoring implementation of legislation as well as ensuring successful enforcement by law enforcement bodies. Political neutrality and professionalism of the public administration is not fully ensured.

Montenegro signed the Protocol of Cooperation on the Creation of the Regional School for Public Administration in May 2006.

The Ombudsman's office has initiated a number of valuable activities aimed at enhancing visibility and awareness, targeting both the population at large and specific stake-holders. His annual report for 2005 notes improvements regarding cooperation with the public administration and compliance with his recommendations compared to 2004. Cooperation with the Ministry of Interior is positive. According to the report, the Office dealt with 707 cases in 2005, out of which 575 were new cases and 132 were taken over from 2004. 299 cases concerned the work of the Courts.

Implementation of local government reform continued. The process was positively assessed by the Council of Europe in its monitoring report of January 2006. A number of activities focusing on local government legislation and on the strengthening of administrative capacity are under way, according to the Work Programme for Better Self-Government. The Government plans to set up a coordination body to coordinate and monitor the overall decentralisation process. Its focus will be to clarify the competences of local self-government bodies and issues of financing. The Code of Ethics for Civil Servants and public employees

also applies to local authority officials. Overall, administrative and management capacities of the local authorities have been strengthened.

Future work in the area of decentralisation should continue to strengthen local democracy and upgrade the administrative capacity of the municipalities. The financial management capacity of the municipalities, including public procurement, should be further improved.

Overall, efforts have been made on the side of the Government to upgrade the administrative capacity of Montenegro. But much remains to be done, notably in the areas of transparency and accountability, financial control, public procurement and budget management as well as management of public assets and licensing procedures. Appropriate resources need to be allocated to match the ambitions of Montenegro in this area. For the successful implementation of the SAA, Montenegro needs to upgrade its administrative capacity in the areas covered by the agreement. Particular attention should be paid to enhancing administrative capacity and law enforcement in the area of justice and home affairs, in particular concerning the fight against corruption and organised crime, as well as the protection of personal data.

Judicial system

The legal framework for the operation of the Montenegrin judicial system has gradually been put in place since 2001 and includes procedural criminal and civil legislation. The basic features of the judicial system are governed by the current Montenegrin Constitution of 1992, guaranteeing the independence of the courts. The court system is regulated by the 2002 Law on Courts. The courts are financed by means of a separate budget, which is adopted by the Parliament on the basis of a governmental proposal. The budget allocated to the courts in 2006 is almost € 8.5 million (around 0.5% of the GDP). The budget for the Prosecution is adopted by the Government on the basis of a proposal by the Prosecutors' Council.

Currently there are 225 Judges in Montenegro, 15 First Instance Courts, 2 Superior Courts, 2 specialised Commercial Courts, 1 Administrative and 1 Appellate Court. The Constitutional Court is also part of the judiciary, with a specific competence. There are also 85 prosecutors including one Chief State prosecutor with six deputy prosecutors, two Higher Court prosecutors, thirteen Basic Court prosecutors with 60 deputy prosecutors of general jurisdiction, as well as one prosecutor and one deputy prosecutor specialised in Organised Crime. However, comprehensive data on the efficiency of the courts including statistics are missing.

The Law on mediation was adopted and it is being implemented on a pilot basis at the Court of First Instance of Podgorica.

The government has recognised the need to further reform and upgrade the judicial system in line with European standards and the European Partnership. The Government has initiated a new Judicial Reform Strategy, which is still under preparation. The draft Strategy addresses the independence and efficiency of the judicial system, accessibility of the courts, education of judges and prosecutors and confidence in a judicial and legal system free from any potential political interference. This direction was confirmed at a high-level public hearing on judicial reform held in June 2006. The Minister of Justice, the President of the Supreme Court and the Chief State Prosecutor were present as well as judges, prosecutors, lawyers, NGOs and representatives of the EU and other international organisations. Reform plans need to be finalised and resources need to be allocated for implementation.

Current activities are still governed by the Judicial System Reform Project for the period 2000-2005. Recent steps include the adoption of the Law on Judicial Education and the Law on Notaries, steps for the implementation of the law on mediation and the creation of an office in the Supreme Court for the fight against organised crime. The Judicial Education Centre will become an organisational unit of the Supreme Court according to the Law on Judicial Education, which will enter into force on 1 January 2007. Specific funding for training will be allocated under the budget for the judiciary, whereas accommodation space for the Centre has been provided. The Centre will provide initial, specialised and continuing education both to judges and prosecutors.

However, a number of issues need attention. Judges and prosecutors are proposed by the Judicial Council and the Prosecutors' Council and elected by the parliament, according to the Constitution and the Law on Courts. The Judicial Council is a body appointed by the parliament and chaired by the President of the Supreme Court. The Prosecutors' Council is chaired by the Chief State Prosecutor. The parliament is also involved in disciplinary proceedings and in dismissals of judges and prosecutors. Parliament's involvement in personnel management in the judiciary raises serious concerns for the independence of the judicial system. There is a clear risk of political interference in appointments and dismissals.

The financing of the judicial system needs to be addressed in a comprehensive manner in order to enhance the efficiency and independence of the judiciary.

The implementation of the criminal and civil legislation is still hampered by the limited capacity of judicial professions and relevant administrative structures. There is also only limited interest in judicial vacancies. The efficiency of the work of the prosecutors in the criminal field is additionally hampered by their obligation to represent the state in property and legal matters.

Before independence, judicial cooperation with Serbia was performed on the basis of a Memorandum of Understanding between the two Ministries of Justice from 2004. This implied mutual recognition of court decisions in both civil and criminal matters. Following independence, the judicial cooperation between Montenegro and Serbia and recognition and enforcement of court decisions, will have to be regulated by a bilateral agreement. The Ministry of Justice of Montenegro will have to upgrade its capacity for international judicial cooperation.

Overall, in spite of some progress in terms of continuous strengthening of the judiciary, the lack of confidence in the system and concern over the level of political influence exercised over the judiciary are still high.

Anti-corruption policy

Some progress can be reported regarding Government activities to enhance the fight against corruption. An Action Plan to implement the Strategy against Corruption and Organised Crime of July 2005 was adopted by the Government in August 2006. According to the plan, the specialised prosecutor for the fight against organised crime will also be responsible for prosecuting and investigating corruption cases. A specialised unit will be set up in the Police (Ministry of Interior). A commission will monitor the implementation of the action plan, which was developed in close coordination with the Council of Europe and with involvement of NGOs. Key measures are derived from the most important international documents, including GRECO (Group of States against Corruption), the PACO Impact project of the

Council of Europe, as well as the European Partnership priorities. The Action Plan should be implemented by intensifying operational cooperation among all relevant institutions and with NGOs.

The Directorate for the Anti-corruption Initiative has a strategic role and is the central government body in charge of prevention and coordination of anti-corruption activities. Authorities have started to report on corruption cases. In the last annual report of the Chief State Prosecutor there are data about key categories of corruption cases (including passive and active bribery, abuse of office and embezzlement). The Law on free access to public information has been adopted.

Montenegro has continued to participate in the Council of Europe's GRECO initiative.

However, the progress on implementation on the ground is still slow. Corruption continues to be a widespread problem. The causes of corruption are related to shortcomings in the transition process and the frequent abuse of administrative procedures. The overall legal and administrative framework for the management of public assets contains loopholes which allow corrupt activities to take place. Privatisation, concessions, construction and spatial planning and public procurement are examples. The lack of guarantees for appropriate control over state institutions and the influence of organised crime in certain spheres of economic and social life further limit the capacity of the state to fight corruption successfully. The lack of an appropriate legal framework to deal with the conflict of interests of officials has a crucial impact. The capacity of the authorities to effectively monitor, prosecute and try corruption cases remains limited and so the total number of persons convicted also remains low.

The Montenegrin Parliament failed to amend the Law on Conflict of Interest. The existing law contains problematic provisions and needs to be substantially reviewed. The laws on political parties and their financing are being implemented with difficulty. Political parties failed to observe the legal deadlines and procedures for reporting financial assets and the financial management of electoral campaigns. Further training of all relevant agencies is needed with a view to fully implement the UN Convention on corruption.

Overall, in spite of some progress in particular in the area of the adoption of strategic and planning documents and in investigation of corruption cases, the situation concerning the fight against corruption calls for urgent action in order to achieve results on the ground. Furthermore, all bodies involved in the fight against corruption need to have sufficient resources and properly trained staff.

2.2. Human rights and the protection of minorities

Observance of international human rights law

The former Serbia and Montenegro State Union was a signatory to all major international human rights instruments, including the European Convention on Human Rights and Fundamental Freedoms. Pending its accession to the Council of Europe Montenegro committed itself to respecting and implementing all the Council of Europe conventions that had been signed and ratified by the State Union of Serbia and Montenegro. It also became a party to other agreements by which the State Union was bound. In June 2006, Montenegro became a signatory or a party to the Council of Europe Conventions opened to non-member States. This applies to the European Convention for the Prevention of Torture and Ill-treatment as well as to the Framework Convention for the Protection of National Minorities and the agreement establishing the Venice Commission. Retroactive application is foreseen

for Conventions that are restricted to Council of Europe member States, such as the European Convention on Human Rights.

The future Constitution (apart from defining the framework for protection of human rights) should provide for the primacy of international law over the domestic legal order as well as the direct applicability of signed international human rights treaties.

Civil and political rights

Pending the adoption of the new Constitution, Montenegro has already developed a set of legal acts on the protection of human rights. These are based on the Charter on Human and Minority Rights and Civil Freedoms of the Constitutional Charter of the former State Union of Serbia and Montenegro.

In the area of the **prevention of torture and ill-treatment**, efforts have continued through education for the relevant bodies of the administration and the judiciary. In May 2006 the European Committee for the Prevention of Torture published a comprehensive report following a visit to the former Serbia and Montenegro in September 2004. Regarding Montenegro, it noted generally good cooperation by the authorities and unhindered access to the facilities, with the exception of one police station. The report noted that persons in police custody run a significant risk of being ill-treated especially when being interrogated. Numerous allegations of ill-treatment were reported. Material conditions in police detention facilities were found unsatisfactory and implementation of basic safeguards against ill-treatment were insufficient, such as access to a lawyer and a doctor, and notification of detention to relatives. The Committee noted that there was a severe shortage of staff in prisons as well as overcrowding of prisoners and poor material conditions. The Committee established a set of recommendations to prevent and sanction ill-treatment.

Cooperation between the Ombudsman and the Ministry of Interior has improved. In total 13 cases involving ill-treatment were received in 2005. The necessary measures were taken in all cases referred to the Ministry, including disciplinary procedures or criminal charges. The investigation is ongoing concerning the incident that took place in September 2005 in Podgorica Detention Facility involving the beating up of a number of detainees. The Ombudsman noted that the proceedings are slow.

However, no progress has been made by the authorities in reacting to the cases brought by the UN Committee against Torture.

As regards **access to justice**, a system of free legal aid has not yet been introduced. Some provisions exist for serious criminal cases and in case of financial hardship. In civil cases, some aid is available to meet costs. However, the existing provisions are not fully implemented in practice.

The situation of the **prison system** is a serious problem in Montenegro. Recent efforts to improve prison conditions included the completion of new facilities for a prison hospital and the introduction of improved security equipment. A new Training Centre was established to improve the skills and expertise of prison staff.

However, both the Ministry of Justice (regulation of penalties) and the Institute for the Execution of Criminal Sanctions (execution) still face problems. The provision of psychiatric care for detainees has been problematic and may require the creation of new facilities. The issue of separation of prisoners has been addressed to some extent as there is now a total

separation between those who serve sentences of less than 6 months and those who serve longer sentences. Further improvements are still needed in prison conditions for vulnerable groups (in particular minors) and a separation of those involved in organised crime cases.

There is also a need for a total overhaul of the probation/parole system. There is a system where prisoners can be released on parole but they can not yet combine parole with probation. Supervision of prisoners who are out on parole or are released as part of a reward system has serious shortcomings. Montenegro would need to build up a probation officers organisation; in which case it would be interesting to consider conditional sentences combined with probation as an alternative to imprisonment.

As regards **freedom of religion**, the constitutional guarantees of freedom of thought, conscience and religion are generally respected. There have been no significant incidents on religious grounds in Montenegro. There is a Commission for religious issues, operating under the responsibility of a Minister without Portfolio, and the Constitutional Council for the protection of minority groups, headed by the President of the Republic. The latter is however largely inactive. A new law on restitution of church property is under preparation. However, the legislation regulating the status of religious communities is obsolete and needs to be updated.

Regarding the **freedom of expression** (including media) the 2005 legislation on free access to public information is being implemented with mixed results. The State administration published various guides for free access to information. The Government Secretariat-General and most Ministries published information bulletins.

However, no efforts have been made to educate civil servants and senior managers in charge within the administration and other bodies including the judiciary. There is extensive referral to exceptions such as state or commercial secret, which limit access to information in practice. The media continues to suffer from occasional political interference. The Radio and Television of Montenegro has not yet been transformed into a genuine independent public service, although in legal terms the transformation has been completed. The appointment of civil society representatives to the Board has been delayed. Political controversy over the independence of Radio and Television of Montenegro during the referendum process resulted in the creation of an ad hoc parliamentary committee to deal with media monitoring. The legislation regulating media concentration has not yet been adopted.

Although defamation remains a criminal offence, fines have replaced prison sentences. However, fines are often reported to be disproportionately high and prison sentences of up to 6 months are still applied. This happens in cases where an individual is unable to pay the fine imposed by the court. The number of defamation cases brought before the courts is high, with 90 cases pending before the Basic Court of Podgorica.

Montenegro has a satisfactory legal framework for the activities of **civil society organisations**, although fiscal aspects are not fully covered. NGO representatives are involved in the preparations of a platform for cooperation between the Government and civil society. The Parliament has often invited NGOs to attend sessions. The Ministry of International Economic Relations and European Integration has signed a memorandum of cooperation with NGOs focusing on information and communication. NGOs are mainly active in the social field, including protection of vulnerable groups, and on election observation. They are increasingly active in the area of European matters and training of NGO representatives, academics and the public sector.

However, the administration continues to show insufficient understanding of the genuine role of NGOs in a democratic society, which also involves criticism of the government. Following the proclamation of independence of Montenegro, a group of leading NGOs called upon the government to fully implement the European Partnership priorities. They also asked to be included in consultations on the drafting and adoption of the future Constitution.

Economic and social rights

Legislation and practice in the field of social rights is largely in line with the provisions of the revised European Social Charter. Montenegro has been a signatory to this Council of Europe instrument since March 2005.

As regards **women rights**, there are no legal restrictions to the access of women to public positions. There is a parliamentary Committee for Gender Equality as well as a Government Office, which prepared an Action plan for Gender Equality in 2005. A Gender Equality Act is currently being drafted as well as a new Family Code.

However, the existing legal framework does not provide sufficient protection from gender-based discrimination in particular in the labour market. The representation of women in political life is limited. The political parties failed to respect the legal guideline to include at least 30% of women among candidates in parliamentary and local elections. Montenegro does not yet have family protection legislation in line with European standards. The high level of domestic violence continues to be a source of concern, as well as the inadequate legal framework to deal with this problem. The police often treat such cases with indifference. Montenegro is mainly a transit and destination country for women and girls trafficked for forced prostitution. Trafficking and forced prostitution are sanctioned in the new criminal legislation as specific offences.

As regards **children's rights**, the former State Union was a signatory to the UN Convention on the Rights of the Child. In Montenegro, a new Law on Protection of the Child and Social Protection was adopted in 2005. The corresponding action plan covers the period until 2010. A centre for children with special needs has been opened in line with the plan and another centre is envisaged for 2006. Two teams to protect children from abuse and neglect were established at municipal level with an additional eight envisaged. However, there is a need to adopt a new family law, as the existing one is not in line with international and Council of Europe standards.

As regards **socially vulnerable or disabled persons**, the Employment Office provides specific incentives to employers hiring disabled persons, in line with the Law on Employment. Results have so far been limited. In practice, disabled people often remain subject to discrimination and their access to social services remains difficult. A new Law on Vocational Training and Employment of Disabled Persons is in preparation.

Regarding **property rights**, restitution of property is covered by the Law on Restitution of Confiscated Property Rights and Compensation which was adopted in 2004. The Government has passed a Decree on Creating a Fund for Compensation. Twenty one municipal commissions for restitution and compensation are functioning. Municipal commissions have adopted decisions involving the payment of compensations to amount of around 26 million Euros in total. The Compensation Fund paid around 6 million Euros in cash and state bonds to former owners. Payments are made in instalments. Complaints have been submitted by former owners regarding the earlier privatisation of real estate property which is subject to restitution.

Minority rights, cultural rights and the protection of minorities

The Framework Convention for the Protection of National Minorities and the European Charter of Local and Regional Languages were ratified by the former Serbia and Montenegro. International agreements were signed with countries in the region (Hungary, Romania, Croatia and former Yugoslav Republic of Macedonia). After the proclamation of independence, Montenegro is in the process of reviewing its legal obligations and defining the institutional and legal set-up for the protection of minority rights.

In April 2006, a new Law on Minority Rights and Freedoms was adopted by the Parliament. This law provides for a general framework for the protection of minorities and affirms the multi-ethnic character of Montenegro and Montenegrin society. This includes non-discrimination of ethnic and other minorities, use of language, free association and participation of minorities in public and social life. It also envisages the establishment of minority National Councils, as well as a Republican Fund for Minorities. However, the adoption of this law was marked by a lack of political consensus, as the opposition abstained from voting. Following a motion launched before the Constitutional Court, questioning some provisions of the law providing for affirmative action in the area of elections and parliamentary representation of minorities through *a priori* allocation of seats, the Constitutional Court annulled the related provisions.

The October 2005 Law on the Capital Podgorica foresees the possibility for the Albanian majority community living in Podgorica's Tuzi neighbourhood to be granted limited management competences. However, the law has still not been applied and is awaiting the adoption of provisions concerning the city's status.

Work has continued on the integration of the **Roma**. The Government adopted an Action plan for the Decade of Roma Inclusion 2005-2015. It has appointed a National Coordinator for its implementation. However the situation of the Roma remains precarious. There is continuing discrimination against Roma people, whose economic and social conditions are difficult. The percentage of Roma living in poverty is four to five times higher than the national average. There are no reliable statistics about the actual number of Roma. Funds remain scarce and the authorities rely heavily upon donor support.

The Referendum of Independence held in Montenegro on 21 May 2006 and the subsequent dissolution of the State Union of Serbia and Montenegro will have an impact on the future legal status of the **internally displaced persons and refugees** currently living in the territory of Montenegro. Persons originating from Kosovo will be particularly affected. According to the latest UNHCR data (June 2006), the total number of refugees and internally displaced persons in Montenegro is 26,193. The new institutional and legal framework in Montenegro is expected to continue adequately provide legal protection for these persons. Pending the adoption of the Law on Asylum the Montenegrin Government took the commitment that independence will not adversely affect the situation of displaced persons and refugees. Montenegro has adopted a national strategy providing for either repatriation (or removal to a third country) or local integration.

However, progress on the ground is limited. Serious obstacles remain concerning labour matters and related rights for refugees and displaced persons who opt for local integration.

Overall, Montenegro needs to clarify and strengthen legal provisions relating to minority rights and the protection of minorities in its new Constitution, in line with European standards.

2.3. Regional issues and international obligations

There are no major problems in Montenegro's compliance with the **Dayton/Paris Peace Agreement**.

Cooperation with the **International Criminal Tribunal for the former Yugoslavia (ICTY)** is now an international obligation for Montenegro proper following its independence. It also remains an integral part of the EU's political conditionality under the Stabilisation and Association process. Following the proclamation of independence, Montenegro has pledged its commitment to full cooperation with ICTY. The cooperation of Montenegro with ICTY is currently satisfactory, according to the latest indications from ICTY.

However, as regards domestic trials of **war crimes**, the trial concerning the deportation of a number of Bosnian refugees in 1992 is still ongoing. Complaints are also being filed in the Podgorica civil court against the Montenegrin authorities. Reparations, including compensation, are being sought on behalf of some of the families of more than 80 Bosnian civilians. Having fled as refugees to Montenegro during April and May 1992, these civilians were subsequently arrested and reportedly handed over by the Montenegrin police to police and military forces of the de facto Republika Srpska. The Supreme Court has ruled that these civil cases should not be allowed to proceed until the conclusion of investigation against six low-ranking police officers suspected of involvement in the deportation.

Montenegro is preparing its own act on cooperation with the **International Criminal Court**. It will be important that Montenegro continues to fully support the ICC and the integrity of its statute, in line with relevant EU decisions.

Regional cooperation and good neighbourly relations form an essential part of the process of Montenegro's moving towards the European Union.

Montenegro is an active participant in the Stability Pact and other regional initiatives such as the Central European Initiative and the Adriatic Ionian Initiative. Montenegro is committed to the establishment of a new, more regionally owned cooperation framework. Following independence it submitted an application for membership to the Central European Initiative, the Adriatic Ionian Initiative and the South East Europe Cooperation process. The procedure for its accession to these organisations is under way. Montenegro is taking part in the negotiations aimed at the establishment of a regional free trade area within the framework of an enlarged and amended Central European Free Trade Agreement (CEFTA). Montenegro is a signatory to the Energy Community Treaty, which entered into force on 1 July 2006. It has ratified the Treaty recently. It also signed the European Common Aviation Area Agreement in June 2006.

Montenegro has been contributing to regional stability. Progress achieved in negotiations with Serbia on pending issues resulting from the dissolution of the State Union is particularly significant in this respect. The Agreement between Serbia and Montenegro on membership into the International Financial Institutions and the distribution of financial assets and liabilities of 10 July 2006 paved the way for Montenegro's accession to those organisations. Further agreements in the area of social security will assist freedom of movement between the two countries.

Montenegro has indicated that it fully adheres to the United Nations Security Council Resolution 1244 on Kosovo.

Montenegro has gradually been establishing bilateral, good neighbourly **relations with all the countries of the region**, following its proclamation of independence. Practical cooperation on the ground is satisfactory especially in the areas of border control, energy supply and environmental protection. Bilateral memoranda of cooperation in internal affairs and the fight against organised crime have been signed with a number of partners including most neighbouring countries. Political contacts are frequent and based on mutual understanding and respect. Cross-border cooperation is one of the current objectives of local government reform.

3. ECONOMIC CRITERIA

3.1. Introduction

In examining the economic developments in Montenegro, 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.

3.2. Assessment in terms of the Copenhagen criteria

3.2.1. The existence of a functioning market economy

Economic policy essentials

The government adopted an Economic Reform Agenda for Montenegro (2002-2007), which provides the guidelines and the macroeconomic framework followed by the authorities. The International Monetary Fund (IMF) and the World Bank fiscal frameworks and targets are adopted as references. Moreover, authorities at all levels recognise the need to harmonise with EU directives and recommendations as common goals. However, the adoption of proposed legislation often suffers significant delays in the parliament. Overall, the country has maintained a broad consensus on the essentials of economic policies.

Macroeconomic stability

In 2005, real GDP rose by 4.1%. This reflected strong growth in tourism and financial services and construction particularly, whereas industrial production declined. In the first half of 2006, GDP grew by 6.5% in real terms. Almost all sectors registered growth over the same period in the previous year, but especially civil engineering and tourism. Industrial production fell by 1.9% in 2005, reflecting problems in some key enterprises which have a large effect on the economic activity of Montenegro. This concerns the lack of funds for carrying out repairs and maintenance at the coalmine complex in Pljevlja, with the resulting shortage of coal to feed the associated power plant. The reversal of the privatisation of the Steelworks Niksic also had an effect, following the new owner's withdrawal in November 2005. In the first half of 2006, industrial output rose 2.9% year-on-year, driven by strong performance of mining and quarrying, industry and utilities. The manufacturing industry recovered in June, registering a 2% year-on-year growth, following two months of contraction. The highest improvement was recorded, in the industrial sub-groups of food manufacturing and wood production, as in 2005.

The current account deficit widened to 12.2% of GDP in 2005, mainly due to an increase in the trade deficit, which rose to 34.2% of GDP, after 27.1% in 2004. This widening was driven by robust domestic demand, especially consumer goods, and a limited export capacity, mainly consisting of low-processing products. In contrast, the balances of services, income and transfers reached a combined net surplus of 22.1% of GDP, due to growing tourism activity and workers remittances. The privatisation of Telekom Montenegro, Podgorica Aluminium Plant and Podgoricka Banka contributed to a record FDI inflow of 22.8% of GDP in 2005. This more than offset the current account deficit. Moreover, the current account deficit further deteriorated in the first quarter of 2006. It registered a deficit amounting to 13.1% of GDP, induced by investment-related increases in imports of services. By contrast, exports of goods rose sharply by 43.3% year-on-year, whilst imports of goods rose by 18.6%. The ratio of exports to imports reached 49.2%, up from 42.5% in 2005. Foreign direct investment (FDI) amounted to €173 million in the first half of 2006. The previous year's record high FDI were mostly achieved through privatisation receipts, whereas in 2006, they are mostly from additional investments following privatisation operations, as well as from greenfield projects.

Important discrepancies exist between the different sources and measurement of unemployment. The registered unemployment rate fell to 18.6% in 2005 from 22.3% at the end of 2004, and recorded 15.7% in July 2006. By contrast, unemployment according to international definition was up to 30.3% in autumn 2005 (LFS data), from 27.7% in the same period of 2004; that is an increase of 8.4%. This however is likely to overestimate the actual level of unemployment as workers with non standard contracts (e.g. part-time jobs, occasional/casual work, jobs with seasonal, temporary or fixed term contracts) are not recorded as employed by the national LFS. In the same period, the decline of employment (LFS) apparently accelerated. Unemployment is dominated by very long-term unemployment and remains chronic among young people (nearly 60% of the 15-24 years old population, according to the LFS). Overall, unemployment remains high and there is a mismatch between employers' needs and workers' skills.

Inflation has remained relatively subdued. Retail price inflation registered 2.3% on average during the first half of 2006, down from 3.4% in 2005. During the first six months of 2006 industrial prices rose by 2%, agricultural products' prices by 7.2% and services' prices by 1.3% year-on-year. Overall, prices of goods have remained higher in the period from January to June 2006 by 2.3%.

Montenegro has continued to use the Euro as legal tender. The only monetary policy instruments are reserve requirements, and the issuing of treasury bills as an indirect possibility to influence interest rates. The Central Bank changed reserve requirements for banks to 19% for demand deposits and term deposits with up to 90 days maturity on 1 February 2006. This was raised to 5% for term deposits with maturity of more than 90 days, but less than one year. Money supply (broad money) growth accelerated to 53.3% year-on-year in June 2006. This increase and its low impact on inflation reflect the ongoing financial deepening process in the country.

The general government deficit slightly widened in 2005 to 2.9% of GDP from 2.6% in 2004. In 2005 the budget benefited from exceptionally high privatisation receipts. The share of VAT in total tax revenues remained substantial at 29.3%. Fiscal reforms have been accelerated, including the adoption of a centralised Treasury, and a new tax system. Budgetary revenues are further increasing, as several laws with a fiscal impact entered into force in January 2006.

In the first half of 2006 the budget recorded strong revenue growth of 29.7% year-on-year and exceeded the budget plan by 13.5%. VAT proceeds were 31.7% above the target and contributed to around 50% of total revenues. However, excise revenues and personal income tax revenues were lower than expected, 6.1% and 1.9% respectively. Meanwhile, budget expenditures only grew moderately by 1.6% year-on-year. Overall, the fiscal position tightened and a budget deficit of around 0.6% of GDP was recorded during the first half of 2006, although the size of public expenditures remains relatively high.

Total public debt was 39.9% of GDP at the end of June 2006. This was equivalent to 703 million (including public and socially owned enterprises). General government debt further decreased in 2005 to 42.6% of GDP, while debt service rose to 6.4% of GDP, twice the amount of 2004. Government debt is composed of 27% domestic and 73% foreign liabilities, the latter mainly concerning the World Bank Group. In July 2006, Montenegro reached an agreement with Serbia on the division of financial rights and obligations of the former state union. The agreement confirmed the previous estimates of the debt levels. Overall, the macroeconomic policy mix is not completely appropriate. The general government deficit widened to a relatively high level against the backdrop of falling wage competitiveness of the export sector and rising external imbalances.

Free interplay of market forces

In May 2006 entered into force the Law of cessation of the law on social control of prices. Only a small number of products or services relating to natural monopolies or public and communal utility services are subject to administrative price control. Retail fuel maximum prices are adjusted every two weeks in line with changes of crude oil prices on international markets and exchange rate dynamics of the US dollar against the Euro. The government transferred the control of energy prices to the Energy Regulatory Agency in July 2005, in accordance with new rulebooks. Price liberalization and regulation is almost complete.

The government launched a project for the restructuring of 97 companies to be either privatized or liquidated in 2005. By the end of 2005, some 80% of company capital had been privatized, and 272, of a total of 386 formerly state and social-owned enterprises are now privately-owned. There are still some 67 public and socially-owned enterprises in Montenegro. 15 are still owned by the central government. Information on the financial performance of these enterprises is not made public. Major companies in public ownership include a power utility and companies in the transport sector such as the railways, ports, airports and an airline. The share of land in private hands increased slightly in 2005 to 67.8% at the end of the year from 67.2% at the end of 2004. Overall, there has been further progress in the development of the private sector.

Free market entry and exit

Registration can be performed in four working days by submitting three documents. Two relevant laws were passed in December 2005: amendments to the accounting law brought this law into compliance with international accounting standards, and amendments to the Licensing law aimed at simplifying the registration procedure at local level. However, the business environment is hampered by regulatory obstacles, particularly at municipal level. There are significant price discrepancies for granting licenses for the same purpose. This is especially the case in licenses for land use, where local fees for installing power or telephone

lines in some municipalities are higher than the expected commercial profit. Overall, business registration procedures are quite efficient.

Adequate legal system

The Commercial Court is the main institution for contract enforcement and guaranteeing property rights. More streamlined procedures have improved its efficiency. The initial backlog of more than 2000 cases inherited upon its creation in 2002 was reduced to 219 pending cases in the first half of 2006. In this period, 84% of cases were finalised, 90% of which were resolved within three months. Judges are obliged to solve commercial disputes within 30 days. The capacity of the judiciary to deal with commercial disputes has improved.

Sufficiently developed financial sector

Financial intermediation has deepened. Total credit growth rose by 34% year-on-year at the end of 2005, compared to nearly 40.3% a year earlier. In the same period, deposits rose sharply by 78.2%. Bank lending to the private sector amounted to 19.3% of GDP at the end of 2005, rising from 15.7% at the end of the previous year. The average interest rate spread of commercial banks at the end of 2005 was 6.6%, and narrowed to 3.9% at the end of June 2006. Overall, financial intermediation has improved.

86.2% of the sector is already privatised and only one bank remains to be privatised. A new foreign-owned bank entered the market in February 2006, raising the number of banks to 10. The share of foreign capital in total capital reached 61% in March 2006. The three largest banks account for about 66.4% of the assets. Two banks merged in 2005, creating the second largest bank with a 37.3% market share. The banking sector recorded a profit of € 4.2 million in 2005. However, improvement in the financial performance resulted almost entirely from reducing one bank's losses. The ratio of non-performing loans rose for its part, by almost 2% at the end of 2005. Overall, the banking sector is mostly privately owned and moderately concentrated.

Risk control is largely in compliance with the basic "Basel principles". The Central Bank has strengthened its regulation and supervisory practices. The Credit register became operational in April 2005. However, commercial banks will need to wait until the second half of 2006 or even 2007 for the Central Bank to start exchanging data with them. E-banking services were introduced in Montenegro in 2005. However, further efforts remain necessary to manage and identify country risk and bank transactions. Overall, banking supervision complies broadly with international standards.

The volume of trade on both stock exchanges increased sharply, reaching 12% of GDP in 2005, more than three times higher than in 2004. More than two thirds of the share turnover was accounted for by the shares of 10 companies. The Telekom shares are far ahead of the others. Both Stock Exchanges registered a significant increase in the prices of shares and stock indexes, following the country's independence. Overall, stock market turnover has increased sharply.

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

Existence of a functioning market economy

Macroeconomic stability has been broadly maintained. However, economic growth has remained dependent on a few key sectors and enterprises and external balances have widened.

Sufficient human and physical capital

High dismissal costs of six months average salary and inflexible employment contracts continued to discourage companies from hiring, especially young people. Wage setting mechanisms only concerns nominal wages in a limited number of economic sectors. These factors are compounded by the high tax wedge of about 41% of total labour costs for employers. An increasing number of jobs are of an irregular nature or informal. The number of job seekers continues to be higher than demand at all educational levels. The highest mismatch relates to secondary education, representing 73% of total unemployment in 2005. Overall, labour markets have remained fairly inflexible.

Human resource development is a pressing priority that requires additional efforts. Active measures do not sufficiently address the groups having the greatest difficulties in accessing employment, in particular young people, women and long-term unemployed. ALMP provision remains unbalanced with not enough results enhancing employability and adaptability of those unemployed. Resources are limited and not efficiently allocated.

Data on capital stock and investment in the economy are not available; however, FDI inflows surged in 2005 to 22.8% of GDP compared with just 3.3% in 2004. 51% of FDI were in non-financial services. The robust FDI growth in the manufacturing and financial sectors is a consequence of accelerated privatisation. FDI inflows in 2006 are mostly due to additional investments following privatisation and greenfield projects. Government capital expenditure increased to 3% of GDP in 2005. There is virtually no investment in research and development. FDI inflows have surged overall.

The telecommunications sector is fully privatised. In the energy sector, one of the two hydropower plants is under reconstruction, while the other has obtained a foreign loan for reconstruction. The privatisation process has started of the thermal power plant and part of the adjacent coalmine. The privatisation of the power company is still under preparation. The oil distribution company Montenegro Bonus still remains state-owned. Overall, privatisation of network industries is well advanced.

Adequate sectoral and enterprise structure

There is no information on the sectoral distribution of value added in the economy. The distribution of employment by economic sector in 2005 was 72.1% in services, 19.2% in industry and 8.6% in agriculture. Almost 20% of employment is in the public sector. Employment in industry increased by 1% and decreased in agriculture by 8%. Services increased by 1.1% whereas employment in the public sector diminished by 1.1%. The sectoral composition of employment has continued to evolve.

The number of SMEs increased by 7.1% in 2004 to almost 28,000 at the end of 2005. They generated 62% of GDP in 2005 and accounted for 36.8% of the registered employment. The number of SMEs further grew by 4.5% in 2006, totalling around 30,000 at the end of June. The Self-employment Programme of the Employment Agency financed programmes for a total value of € 3.5 million in 2005, creating some 1,000 new jobs. The agency also trained more than 2,000 persons in the first half of 2006. Support to small and medium-sized enterprises is mainly provided in the form of credits through a programme, which was established in 2005. Overall, small and medium-sized enterprises (SME) further increased their role in the economy.

A new tender for the privatisation of the steel mill was launched in July 2006. The previous buyer withdrew in November 2005 after 16 months' operation. The government cancelled the privatisation contract and took over the mill in January 2006. The government has taken over the total of the steelwork's debt, to facilitate the new privatisation tender. 580 workers have left through the redundancy programme. Other sectors are also in need of major restructuring. These include the railways company, the port of Bar and the power company (EPCG). Overall, some further restructuring is needed.

State influence on competitiveness

Budget transfers to socially-owned enterprises are negligible (1.1% of GDP in 2005), however, debt and arrears from some companies to the government remained significant and difficult to determine. A project initiated by the Government and commercial banks in 2004 has also provided more than 600 loans to SMEs. The tourism sector has benefited from a new reduced VAT rate of 7%, instead of the former 17% rate, since January 2006. Exports are also exempt from VAT. Although publicly-owned enterprises are subject to the same taxes as private firms, the sales of Montenegro Airlines and the postal company are exempt from VAT. Airline ticket sales are considered exports and postal services are considered essential. Under current legislation, foreign investors are treated the same as local ones. Overall, government intervention has diminished.

Trade integration with EU

The share of imports of goods and services rose to 67.1% of GDP (2004: 63.2%), and exports decreased to 44.5% (2004: 45.7%). The commodity structure of exports is fairly concentrated. Exports of raw or intermediate materials, mostly unalloyed aluminium, accounted for 56% of all exports in 2005. 48.9% of total exports went to the EU in 2005. The EU is also the main exporter to Montenegro. 40.3% of total Montenegrin imports came from the EU. Serbia accounted for 36.8% of total exports, (mostly metal products, food, beverages and tobacco), and 34.8% of imports, (principally agricultural and chemical products, and machinery).

Montenegro is also a relatively large exporter of services, mainly as a growing tourist destination. Total tourism revenues amounted to 12.5% of GDP in 2005, and surged by 20% year-on-year in the first seven months of 2006. Preliminary data shows that overnight stays were 14.7% higher than in the same period of the previous year. Overnight stays for foreigners accounted for more than half of this number. Overall, trade openness has slightly risen. The CPI-based real exchange rate vis-à-vis the euro remained roughly stable. However, wages continued increasing in 2005 by 6.7% in real terms, and even by 17% year-on-year in the first half of 2006.

4. EUROPEAN STANDARDS

4.1. Internal market

4.1.1. *Free movement of goods*

Some progress has been made regarding preparations to introduce quality infrastructure. Following its proclamation of independence and the dissolution of the State Union, Montenegro has indicated temporary application of the framework laws on quality infrastructure which were adopted by the former State Union (the Law on Accreditation, the Law on Standardisation, the Law on Metrology, the Law on Technical Requirements and Conformity Assessment of Products). Basic infrastructure exists partially through previously established regional standardisation and metrology branches, which will need to be extended in order to function as national institutes in their respective competencies. Montenegro has indicated readiness to act speedily in this sector and to create a centre for standardisation and a centre for legal metrology. Activities in this field are coordinated by a Committee for Quality which operates under the responsibility of the Ministry of Economy (Department for Quality Infrastructure). Technical support is provided by the Centre for Quality within the Mechanics University in Montenegro.

Concerning **accreditation**, Montenegrin authorities will have to decide whether to rely on other countries' accreditation bodies on a commercial basis or whether to establish its own institution, taking into account economic viability criteria. Montenegrin companies are already addressing foreign accreditation bodies on a commercial basis.

No progress can be reported in the area of **market surveillance**.

Although Montenegro is making progress in its preparations for alignment, no concrete timetable for the alignment of Montenegrin legislation to the Community New or Old Approach Directives exists. Preparations for alignment with the *acquis* in this area are moderately advanced. Besides strengthening the other quality infrastructure institutions there is a need to establish an appropriate market surveillance structure based on adequate product legislation required under the New Approach directives and phase out contradictory pre-market controls. Preparations for alignment with the *acquis* in this area are overall at an early stage.

Progress in the area of **consumer protection** has been limited. Montenegro lacks a comprehensive framework on consumer protection. A draft law has been prepared and has been subsequently commented by EU experts. This text should be revised according to the recommendations of the EU experts and forwarded for adoption by the Parliament. Corresponding administrative capacity and information to consumers should be further strengthened. In this context, the creation of an IT network for market inspectors is of great importance in order to ensure efficient enforcement of consumer protection. Also overall information and awareness of consumers on issues related to consumer protection is very limited. As regards health protection Montenegro has adopted a number of laws, covering health care, contagious diseases and the use of tobacco. In the area of consumer and health protection Montenegro has only just started to prepare to meet the objectives of the European Partnership.

Overall, limited progress can be reported in the area of free movements of goods. Montenegro needs to strengthen its capacity in this field.

4.1.2. *Movement of persons, services and right of establishment*

Progress in the area of **movement of persons** has been limited. The forthcoming adoption of a Law on aliens should clarify rights for the employment of foreigners. Some progress can be reported in the field of the coordination of social security systems with Serbia. Issues related to the movement of services are covered under the ongoing negotiations for accession to the WTO, as well as for an SAA.

Montenegro is following a liberal policy in relation to the provision of **services**.

In relation to **financial sector** regulation and supervision, the legal and institutional framework for banking supervision has been significantly strengthened since the Central Bank started to perform a supervisory function in 2001, in particular with the introduction of new regulations on licensing, minimal capital requirement, asset classification, loan provisioning and limitations on large exposures. Moreover, privatisation of the banking sector has proceeded apace with the three largest banks now majority foreign owned, though the state continues to hold minority equity stakes in six of ten banks. In total, foreign-owned banks account for over 70% of the banking sector's capital. Despite these positive developments, the authorities are aware of the limitations of the current legal framework, notably in relation to the need to improve bank corporate governance and risk management requirements, the procedures for the reorganisation of banks and the Central Bank's enforcement powers including supervision on a consolidated basis. A revised draft banking law and central bank law are under preparation. There are also plans to upgrade the regulatory and supervisory framework in the insurance sector, which is currently *de facto* unsupervised, through the adoption of a new insurance law.

On the **right of establishment** of companies, the duration of the procedure for the registration of a company has been substantially reduced. Furthermore, "silent approval" has been introduced in licensing and registration. Bottlenecks have however been identified at the level of municipalities. The Agency for Development of Small and Medium-sized Enterprises is currently working on the elaboration of a detailed analysis of business barriers, while a draft Law on Licensing is in Government procedure.

In the field of **company law**, all legal entities with a turnover greater than €500,000 are required by law to prepare annual accounts in accordance with international accounting standards. Annual accounts should be audited by licensed auditors in accordance with International Standards on Auditing. The proportionality and enforceability of these financial reporting requirements in the Montenegrin context is open to question. The legal framework also remains incomplete, notably in relation to the designation of a national accounting standard-setting body and in relation to the training and registration of auditors. Moreover, with the notable exception of the banking sector, there is at present limited enforcement of financial reporting rules: the Securities and Exchange Commission does not verify the quality of financial statements for companies falling under its jurisdiction and there is no enforcement of financial statements publication in the company register. There are currently less than 40 licensed auditors in Montenegro.

4.1.3. *Free movement of capital*

Further progress in the area of free movement of capital can be reported. Montenegro has liberalised current payments, as well as direct investment and repatriation of profits. As already reported, further liberalisation of **capital movements** was achieved by means of the

Law on Foreign Exchange from July 2005. Remaining restrictions are based on reciprocity. The acquisition of real estate by non-residents is subject to reciprocity requirement. An inter-banking payment system is in place. Preparations for implementing an SAA in the area of free movement of capital are well on track.

4.1.4. *Customs and taxation*

Some progress has been achieved in the area of **customs rules** during the reporting period. Customs legislation is mostly aligned with the *acquis* except in the areas of rules of origin, transit procedures, customs valuation and customs fees. The amended Customs Tariff Law is in force since January 2006. Simplified procedures have been set up and several requests for granting authorisations have been submitted since the new amended Customs Law was adopted in 2005. A pilot project on the electronic processing of customs declarations was put in place in May 2006. Risk analysis is being introduced and a tender for a programme was launched at the beginning of 2006. The fight against corruption in customs has been somewhat strengthened by the opening of a 24-hour customs helpline in an attempt to combat illegal activities including corruption. 74 disciplinary procedures (for disciplinary and criminal offences) were initiated against customs officials in 2005.

In the field of rules of origin the situation remains problematic. A technical monitoring mission of the Commission services in this area in February 2006 concluded that, while the organisation of customs administration in relation to rules of origin is satisfactory, legislation remains vague. The approach followed by customs officers when issuing and verifying certificates of origin is problematic and producers are not aware of their responsibility on the information they provide on origin.

Twenty duty-free shops were set up in July 2005 on the land border crossing points in Montenegro. As there is no limit to the amount which can be purchased at these shops, there are serious concerns that huge quantities of duty-free excise goods such as cigarettes can be bought abusively in order to be resold in the country or to be smuggled across borders to other countries of the region. This situation provides an additional burden on the customs administration with the performance of extra controls. The Montenegrin authorities gave assurances that these shops would be closed.

Overall, the situation in customs should be improved for Montenegro to be able to conclude and implement the Stabilisation and Association Agreement and the Interim Agreement. The latest EU legislation needs to be taken into account. Customs valuation rules need to be aligned. Customs fees will need to be dismantled. Full implementation of customs procedures in line with EU standards is needed. Regarding administrative and operational practices, improvement is needed in risk analysis and in reinforcing implementation of intellectual property rights legislation. In the field of rules of origin, knowledge of rules of origin by customs officers as well as of producers should be improved, in particular through further training. Current efforts in the area of the fight against corruption in customs need to be pursued and strengthened.

In the field of **taxation**, Montenegro has a VAT system which is broadly in line with the *acquis* and has amended its legislation introducing a reduced rate of 7% that replaced previous exemptions. Until 1 January 2006 a single VAT rate of 17% was applied with a large number of exemptions.

The Montenegro Excise Law, in force since January 2006, is broadly in line with the *acquis*. Excise duties are levied only on the EU excisable goods and discriminatory duties

differentiating between domestic and foreign products no longer exist. The problem of fraud in the area of excise duties, including smuggling, remains of considerable concern.

There were no developments on direct taxation. The legislation provides for a tax rate of 9 % on corporate income and up to 23 % on personal income. Tax reforms have not yet begun to take into account the company tax directives. A Treaty Network based on the latest OECD model should be completed, a European Partnership priority. Montenegro has not yet undertaken a gap analysis aimed at identifying the existing harmful measures which could contradict the principles of the Code of Conduct on business taxation.

Further progress is needed on computerization in the tax administration. Risk analysis has not been fully implemented. The fight against corruption requires reinforcement in order to achieve a non discriminatory application of tax laws.

Overall, preparations in the area of customs and taxation are under way but Montenegro should urgently upgrade its efforts in order to be able to implement commitments under the future Stabilisation and Association Agreement.

4.1.5. Competition

In the area of **anti-trust**, the Law on the Protection of Competition entered into force on 1 January 2006. A set of by-laws on the definition of the relevant market and the form and content of the merger notifications has also been adopted.

The Law envisages a department within the Ministry of Economy as a supervisory authority. This department has already dealt with certain cases of mergers, abuse of dominant position and anti-competitive agreements. Montenegro has to ensure that this department is operationally independent and disposes of appropriate resources.

In the area of **state aid** control, Montenegro is still preparing the relevant legislation. Currently, the monitoring and reporting of allocated aid is carried out by a monitoring team based at the Ministry of Finance. To date, the monitoring team produced state aid inventories for 2003 and 2004. The state aid inventory for 2005 is pending. In view of future commitments under the Stabilisation and Association Agreement, Montenegro needs to strengthen its state aid structure. It needs to set up a system of *ex ante* control of all new aid measures and alignment of existing aid measures, through an operationally independent state aid authority, with the power to authorise or prohibit all aid measures and to order recovery of unlawfully granted aid.

Overall, preparations in the area of competition are moderately advanced. However, in view of forthcoming obligations under the Stabilisation and Association Agreement, Montenegro should address the operational independence of the competition authority and upgrade preparations for the completion of the legal framework for state aids including the establishment of a state aid authority.

4.1.6. Public procurement

Some progress can be reported in this area, with the preparation of a new draft Law on Public Procurement. The draft was adopted in July 2006 by the Government and submitted to the Parliament. This Law provides for the creation of a new institutional framework, in line with EU requirements. Sub-legal acts are in the process of preparation.

The Public Procurement Commission (PPC), responsible for review of appeals in public procurement procedures, also conducted random checks on between 20-30% of procurements specified under the Law and has visited about half of the municipalities to raise awareness about the requirements under the Law. In 2005 there were 109 appeals submitted.

At the present stage, the Montenegrin Public Procurement Law is incompatible with EU legislation in many crucial aspects.

There are 168 nominated public procurement officers in public entities in Montenegro, and about 650 contracting authorities, with a total value of public procurement awarded in 2005 of slightly more than 217 million € (12% of GDP, according to the Central Bank 2002 figures). Therefore public procurement is an important issue from an economic point of view. Allegations of corruption and fraud in the awarding of public contracts need to be seriously addressed by the Government.

Further substantial changes in the Public Procurement Law (including the development of a comprehensive set of implementing regulations) will be required in order to bring it in line with the EC Directives. Substantial work will be required to upgrade the administrative capacity and the systems for monitoring and controlling procurement activities (including financial management and the independent control and audit functions outside the procurement system itself). The Public Procurement Agency should be strengthened and be provided the means to perform its control and coordination tasks. Training on public procurement for both economic operators and procuring entities in accordance with the rules provided for by the new Law will be crucial.

Overall, preparations for alignment with the *acquis* in this area are underway. A substantial strengthening of the legal and institutional capacity of Montenegro in this area will be crucial for strengthening the rule of law and the prevention of corruption. Montenegro should upgrade its efforts to fully implement the corresponding European Partnership priorities and to prepare for implementation of the Stabilisation and Association Agreement.

4.1.7. *Intellectual property law*

Following the proclamation of its independence, Montenegro has started to consolidate the legal base and the administrative capacity to establish a regime for the protection of **intellectual property rights**. The Law on Applying Regulations Settling the Protection of Intellectual Property Rights entered into force in January 2006. This Law introduced into the Montenegrin legal order a set of key intellectual property laws which were adopted in December 2004 by the former State Union and cover authors' rights and related rights, patents and topographies of integrated circuits. Following independence these laws remain in force.

Regarding the implementation of copyright and related rights, right-holder and societies for collective rights, PAM, an organisation of collective management of copyright and related rights of musicians has been established in Montenegro.

Concerning enforcement, some texts have been already adopted by Montenegro in order to implement commitments under the legislation of the former State Union, which have strengthened in particular the customs procedures in relation to goods under intellectual property rights. Montenegro has indicated plans to rely on technical support from Intellectual Property Offices of other countries in the region on a commercial basis for an initial period.

Some enforcement capacity exists in Montenegro. Officials in bodies for protection of intellectual property rights have been trained. Enforcement activities have been intensified as from beginning of 2006, the entry into force of the IPR Enforcement Law allowed to conduct inspection, and intervene in particular regarding copyright violations and the legalisation of computer software. Co-operation between the Montenegrin custom authorities with neighbouring countries would further raise efficiency in the fight against piracy and counterfeiting.

Montenegro will have to accede to all IPR conventions that the State Union of Serbia and Montenegro had signed in the past in order to fulfil its future obligations under the SAA and the WTO.

Overall, the state of preparations in the area of intellectual property is on track. However, alignment with the *acquis* is still at a very early stage in all areas of this chapter

4.1.8. *Social policies*

The overall **employment** rate in Montenegro falls behind the EU average. Unemployment is structural and long-term. Seasonal employment is centred on the tourism, construction and agriculture sectors and where precarious forms of employment contract are common.

There are no specific measures to address youth unemployment, and vocational training is limited. The Employment Agency operates its own centres for vocational training and organises training at the request of employers. Employment rates of those who follow training delivered by the employment service are good (74%).

The Employment Agency has estimated that as much as 30% of the registered unemployed hold jobs in the informal economy.

A 2002 Employment Law provides a framework for employment regulation. Active employment measures, job counselling and vocational training based on the needs of the economy in active cooperation with employers needs to be further developed to tackle long-term unemployment, employment of youth, women and minorities. A review of overall public expenditure on active employment measures should be undertaken in order to determine how existing budgetary resources can be optimized to support employment integration of all key target groups. Medium to longer term perspectives building is also required to upgrade investment in human capital and ensure life-long learning. A particular gap at this stage is non-university, third level education which can directly address adults out of work, returnees as well as those in jobs and where new knowledge and competence will be important for continued employability and better business performance.

No progress has been achieved in the area of **health and safety at work**. The authorities need to take steps to tackle the outstanding issue of weak implementation capacities. The creation of a modern legal framework for Occupational Health and Safety and its consistent implementation are a key factor for social progress.

In the area of **gender equality**, the Labour Act provides only a general non-discrimination formula with no further definition of the concepts of direct and indirect discrimination. Sexual

harassment is not recognised and the principle of equal pay for work of equal value is not explicitly stipulated in legislation. Women participation to the labour market is very low.

In the area of **social dialogue**, the Economic and Social Council established in early 2001 by Government Decree is the first structure tailored to generate social dialogue. However, the stakeholders do not perceive it as an independent, neutral or powerful advocate. The Government should proceed with its plan to set up a revamped version of the Economic and Social Council through the issuance of a law on the Economic and Social Council that addresses its current weaknesses. Significant efforts are being made by the authorities for reform across the **education** system. However, regulation on decentralisation is not being put to good effect given weak capacities at local level particularly in adapting curriculum to local community requirements. Minority communities in particular are not availing of localisation of curriculum option. Integration into the European area of higher education in the context of the Bologna process is on track while a National Qualifications Commission has been established to carry forward policy reform in line with the provisions of the European Qualifications Framework. However, non-university, higher education is very much underdeveloped and represents a critical constraint in the country's life-long learning perspective.

In the area of employment and education Montenegro is advancing, but there is a need to streamline policies and measures and indicate priorities for active employment measures. There is a need to upgrade skills in line with the requirements of the economy.

4.2. Sectoral policies

4.2.1. Industry and SME

Steady but overall slow progress has been noticed in this area.

The Action Plan for the Stimulation for SME Development 2005-2007 was adopted in February 2006 and is in the process of being implemented. Montenegro is implementing the European Charter for Small Enterprises. Due to the Charter Process, SME Policy is well advanced.

Montenegro is now making initial progress with the development of its first SME incubators, one of which is planned for Podgorica and a specific one for wood processing in Rozaje.

The Government has adopted an Export Promotion Strategy in December 2005 and the SME department has been tasked with its implementation. Key sectors are tourism, agriculture and processing industry and key instruments are the development of brands, analysis of market potentials, credit support for projects and increased effort on standardisation.

The SME department is preparing a detailed analysis of existing business barriers. This is a positive initiative. The analysis will feed into the adoption of a new SME Development Strategy 2007-2010, which has been announced for December 2006. However, these preparations are holding up a number of measures which had previously been announced: in particular, the improvement and harmonisation of business licensing systems at municipal level, as well as the introduction of regulatory impact assessments. For licensing systems, a draft law to streamline licensing is under consideration.

On business representation and advocacy, there is limited progress with the setting up of the Forum for Enhanced Permanent Dialogue (October 2005), which includes a number of SME policy stakeholders.

Montenegro has a speedy company registration system with a silence-is-consent rule (4 days), however online registration is not offered yet.

The proposed set up of a national guarantee fund has not yet been realised. This is currently held up in a feasibility study to advise the Montenegrin Government on which financial instruments (micro credit, equity, guarantees etc) are best suited for the Montenegrin situation.

There has been no progress on the development of a first business/technology parks or on the further development of clusters.

On industrial policy, Montenegro does not have an overall economic-industrial strategy. The Economic Reform Agenda of the Government does not specifically address industrial policy issues. There is a need to develop an overall future looking view on where competitive advantages and restructuring needs lie. The steel sector requires restructuring to achieve viability and competitiveness.

Overall Montenegro has moderately advanced in implementing the European Partnership priorities in this area.

4.2.2. *Agriculture and fisheries*

Some progress has been achieved by Montenegro in the area of agriculture in terms of policy development. However, final adoption of strategies and key legislation and its respective implementation is lagging behind. A "Strategy on Food Production and Rural development – Montenegro's Agriculture and the European Union", defining the future course of development of Montenegrin **agriculture** in view of further approximation to the *acquis* and integration to EU markets, was adopted. Progress has been registered in the preparation of a food safety strategy. A new draft wine law has been prepared.

In the food safety and **veterinary** area, a food safety law, a law on animal welfare and a new veterinary law are still to be adopted. The reorganisation of food-chain laboratories and sanitary inspection is still pending the adoption of relevant legislation. Animal identification and setting up of the animal registration system has not started. Good progress can be reported in the **phyto-sanitary** sector where a new law on plant health was adopted in May 2006. Laws regulating seeds and seeding material for agricultural plants and pesticides have been adopted. Their implementation will require the establishment of a separate phyto-sanitary directorate with functional independence. Veterinary and phyto-sanitary services, however, need to be additionally equipped and trained in order to be able to control the enforcement of legislation.

In July 2006, the Government adopted a Draft Fisheries Strategy and proposed it for public debate. The Draft puts forward solutions aiming at ensuring protection and sustainable development of freshwater and sea fisheries and protecting consumers, in accordance with the EU standards. Once the Strategy is finalised and adopted, its implementation will require serious investment in human and budget resources.

Preparations in these sectors are under way, but there is a need for serious strengthening of the administrative capacity, in particular in the veterinary and phyto-sanitary sectors.

4.2.3. *Environment*

There has been some limited progress in Montenegro's efforts to approximate with European standards in the environmental area. Montenegro has pursued approximation to EU environmental legislation, with important steps forward as regards horizontal legislation (environmental impact assessment, strategic environmental assessment), integrated pollution prevention and control and waste management.

Progress has been made as regards horizontal legislation. The Law on Environmental Impact Assessment (EIA) and the Law on Strategic Environmental Assessment (SEA) were adopted in December 2005, but will enter into force only on 1 August 2008. Montenegro is progressing on with the adoption of by-laws and implementing regulations of the Law on Environmental Impact Assessment. Both the EIA and the SEA laws foresee public access to environmental information, public participation in decision making and access to justice. The provision of information to a third country in case of trans-boundary effects of a project is also an obligation in both laws. The Environmental Inspectorate is in charge of supervising the implementation of the Law on Environmental Impact Assessment. In the area of climate change, neither the UN Convention to Combat Desertification nor the Kyoto Protocol to the UN Framework Convention on Climate Change has been ratified. However, preparations are under way regarding the ratification of the Kyoto Protocol. In general, uneven progress has been made towards ratification and implementation of respective international conventions in the field of environment. Further efforts are needed.

A comprehensive National Strategy on Sustainable Development and a Strategy for Integrated Management of Coastal Areas are under preparation and should be adopted by the end of 2006.

Progress has been made in the area of Waste Management with the adoption of the Law on Waste Management in December 2005, although it will not come into force until 1 November 2008. By-laws related to waste management should be adopted in a period of 18 months following the adoption of the law. Implementation of the Strategic Master Plan for Waste Management, adopted in 2005, has begun. Progress in the implementation of the solid and water waste strategies is limited.

Limited progress can be reported in the area of water quality. A new Law on water should be adopted in 2006. The Master Plan on Water Supply in the Coastal Region and the Municipality of Cetinje was adopted in July 2006. Implementation of the Master Plan for Waste Water Management depends on the establishment of an adequate institutional mechanism for this purpose. Poor water and sanitation remain key challenges for Montenegro.

Progress can be reported in the area of Integrated Pollution prevention and Control (IPPC). The Law on Integrated Pollution Prevention and Control was adopted in December 2005, but will only come into force on 1 August 2008. Public access to environmental information, public participation in decision making and access to justice have been included in the Law. The relevant secondary legislation and implementing regulations are under preparation. The existing installations are required to comply with IPPC requirements by 2015.

No new legislative developments are to be reported on approximation with EU standards in air quality, nature protection, chemicals and genetically modified organisms.

Implementation capacity has slightly improved, notably through continued and on-going capacity building of the relevant bodies, the adoption and implementation of strategies and master plans, and the adoption of financing plans as regards investments required to meet European standards and to tackle pollution at existing hot-spots. However, administrative capacity is weak. It is affected by the lack of sufficient competent staff in the Environment Sector of the Ministry of Environmental Protection and Physical Planning and lack of satisfactory coordination among the bodies having an involvement in environmental protection issues. The lack of implementation capacity at local level and the poor coordination between central government and local government further limit enforcement capabilities. A persisting weakness impairing enforcement of environmental legislation is the low awareness among the judiciary of environmental issues, which leads to inexistent or insufficient sanctions in case of infringements or criminal acts of an environmental character. The establishment of the Environment Protection Agency (planned by the end of 2006) should play a key role in the rationalisation in the management and transformation of institutional structures. This should contribute to the strict separation of policy and legislation tasks, which will remain in the Ministry, and implementation issues, which will be the responsibility of the new Agency. However, it is unclear if the resources to be allocated to the Agency will be sufficient.

Overall, whereas activities in this area are under way, the concrete results in terms of increased capacity have not been fully apparent yet.

4.2.4. Transport policy

Preparations in the field of transport have started but remain at an early stage.

In the area of **transport networks**, Montenegro is actively participating in the development of the Core Regional Transport Network and in the South East Europe Transport Observatory (SEETO), in particular by approving the first Rolling Five Year Multi-Annual Plan 2006-2010 (MAP). Continued cooperation in the framework of SEETO is required in the context of the annual revisions of the plans in order to make further progress on the definition of regional priorities and the coordination of investments.

The Republic of Montenegro's surface transport system, both road and rail, is part of the regional network. The transport network has suffered chronic under funding in the past decade. Conscious of the importance of the network to the future economic success of the Republic, the Government has addressed legislative obstacles to investment by adopting new laws governing transport.

Concerning **road transport**, the Laws on Transport of Passengers by Road, Road Transport of Goods and on Road Safety were adopted in 2005. Implementing legislation has also been adopted. With the establishment of the Roads Directorate and the dissolution of the Directorate for Highways, the market situation should be improved. The Transport Ministry prioritises maintenance over new road construction. This allows separation of investments between infrastructure and operational activities which encourages additional investment from IFIs.

Some progress can be reported in the area of **rail transport** as the restructuring of the Rail Company is progressing. It has been unbundled for accounting purposes, but not yet in legal terms.

In the field of **air transport**, by signing the European Common Aviation Area Agreement (ECAA), Montenegro has undertaken to integrate into the EU internal aviation market and to apply EU aviation standards. This will require the application of the ECAA agreement in practice and the fast implementation of the first transitional phase of the relevant aviation *acquis*, including market access conditions, safety, security, airport policy, environmental and social issues and air traffic control, in line with the European Partnership short term priority.

In the sector of **inland waterways**, Montenegro participates in the work of the International Commission for the Sava basin which started its work in January 2006 aiming to the preparation of re-establishment of the river navigation.

In the **maritime transport**, assessment and strengthening of the administrative capacity are under way, particularly in the field of flag State and port State maritime safety measures. A new legal framework is being prepared involving laws on maritime navigation, ports, maritime safety and security, and sea protection.

4.2.5. Energy

Some progress has been made in the field of energy.

As regards oil stocks and security of supply, no progress has been registered. Montenegro does not hold sufficient oil stocks.

Some progress has been made regarding the electricity and gas sectors. Montenegro has ratified the Energy Community Treaty . However, the adoption of relevant *acquis* for the creation of an effectively liberalised energy market in electricity and gas is underway, notably on electricity tariffs. An Energy Development Strategy to cover the period 2025 is under way. The power utility EPCG has been functionally unbundled, while legal unbundling has not been achieved yet. Tenders for the privatisation of the thermo power plant Plijevlja and for a minority share in the coal mine AD Plijevlja have been completed. No progress was noted regarding state aids to the coal industry. A Strategy for restructuring and privatisation of the power utility (EPCG) has been adopted.

The establishment of the Energy Regulatory Agency has been launched.

Good progress can be reported on energy efficiency and renewable energy sources. Montenegro adopted an energy efficiency strategy and an action plan for its implementation. An Energy efficiency Department has been established in the Ministry of Economy. However, its administrative capacity is limited. A strategy for the development of small hydroelectric power plants has also been adopted.

There has been no particular progress as regards nuclear safety and radiation protection. An appropriate regulatory body needs to be put in place, and the necessary legislation needs to be adopted in order to comply with the Community legislation, in particular regarding the environmental monitoring and the radiation protection in connection with medical and industrial applications, including provisions on waste management and on control on radioactive sources.

Plans for a storage facility for spent radioactive sources have been developed. Montenegro will need to ensure compliance with Euratom Treaty requirements and procedures. Following independence Montenegro needs to accede to the main international Nuclear Safety Conventions.

Administrative capacities in all energy sub-sectors need to be strengthened.

4.2.6. *Information society and media*

Some progress can be reported in the area of **electronic communications and information technologies**. The Strategy for the Electronic Communications Sector was adopted in June 2006. It outlines the necessary steps to establish a fully functioning market and addresses current and future developments leading to a convergence of the different technologies. In this light, it proposes to merge the Agency for Telecommunications and Post and the Broadcasting Agency into a single Agency for Electronic Communications and Post. However, the proposed merger raises some concerns, in particular regarding the current autonomy and independence of the Broadcasting Agency.

As it was reported in 2005, the telecommunications market is formally liberalised but competition exists only on the mobile market (two operators). In order to ensure the opening of the market, the necessary tools to encourage competition (such as carrier (pre-) selection, number portability and local loop unbundling) need to be introduced. Moreover, the interconnection tariffs, due to be reviewed at the end of 2006, are currently very high. Legislative proposals aimed at aligning the legislation to the 2002 EU framework will be drafted using the adopted Strategy as a basis.

No Voice over IP licences have currently been issued, which is largely due to the high licence fees for international traffic. It is essential for the introduction of competition in Montenegro to reduce market entry barriers such as high licence fees as well as addressing further the issue of tariff rebalancing.

The Agency for Telecommunications has in the past supervised steps towards a Reference Interconnection Offer (RIO) from Telecom Montenegro (the fixed telephony incumbent operator), in addition to other activities such as issuing licenses, drafting rule books, monitoring the market and controlling radio frequency systems. The administrative capacity of the Ministry of Economy to execute tasks related to drafting policy and legislation is limited, leading often to the situation where its legal competences are executed by the Agency.

As regards **information society services**, the Council of Europe Convention on Cyber-crime has not yet been ratified and laws on cyber-crime and personal data protection still need to be adopted. The preparations for alignment with the *acquis* on electronic commerce and conditional access services are advancing.

In the field of **audiovisual policy** there has been some progress. The legal transformation of Radio Television of Montenegro into a public service has been completed, but its Programme Board has not yet been appointed. Sufficient guarantees for its independence will have to be provided. It is necessary to update the Broadcasting Development Strategy (especially in the light of the future merger between the authorities for telecommunications and broadcasting) and to adopt a plan for alignment with the audiovisual *acquis*.

The Broadcasting Regulatory Authority of Montenegro is well established, independent from the Government and working efficiently. In the event of a future merger between the Agency for Telecommunications and Post and the Broadcasting Agency, it is important that such a process does not jeopardize the well-established independence and proven efficiency of the Broadcasting Regulatory Authority.

Ultimately, the independence and efficiency of the regulation for the audiovisual/broadcasting sector will be guaranteed if the resources and financing arrangements dedicated to it are sufficient and the political will to introduce and implement European standards is present.

Overall, whereas Montenegro is on track regarding electronic communications, it has made some, albeit rather limited, progress in the field of information society services and media. In the area of electronic communications, the issues related to the legal framework and to the administrative capacity of the Government and the Agency for Telecommunications need to be addressed in the context of the implementation of the Stabilisation and Association Agreement.

4.2.7. Financial Control

Limited additional progress can be reported in the area of public internal financial control. The Budget Law, which is a sound starting point for the development of PIFC, allows for the Minister of Finance to prescribe internal audit procedures and approaches. There is no law on internal audit. An internal audit unit in the Ministry of Finance was established in September 2003. This unit is responsible for internal audits in the Ministry of Finance, other ministries and spending units and municipalities. Customs and the pension fund have established their own internal audit units. Internal audit activities are performed on the basis of an internal audit charter, which has been followed by an internal audit manual, adopted in 2004. After subsequent training during the second half of 2004, internal audits have focused on expenditure of the state budget and state funds. So far 16 audits have been carried out. Some audits have been carried out by request from municipalities. Ex ante financial controls however are not systematic, and budget users are not required to have internal control structures.

Some progress has been achieved in the area of external audit. Since the establishment of the State Audit Institution of the Republic of Montenegro in April 2004 pursuant to the Law on the State Audit Institution, the elements of a system for internal and external financial control have been gradually introduced in Montenegro. The State Audit Institution is appointed by the Parliament, to which it reports. According to its rules of procedure, the State Audit Institution should have a total staff of 37, of which 24 state auditors. However, only six state auditors are currently employed. In July 2005 the State Audit Institution submitted to the Parliament its first annual report. For the financial year 2005 the annual financial statements of the Republic are being audited together with two municipalities and one extra-budgetary fund. In January 2006 the State Audit adopted its annual audit plan. So far only regularity audits have been performed, although the law provides also for effectiveness and efficiency audits. A programme for education and training of auditors is under way. The State Audit institution has engaged in international cooperation and exchange of experiences with other supreme audit institutions in particular with neighbouring countries, and has submitted an application for membership in INTOSAI.

Montenegro will have to substantially update its system of internal and external control. The State Audit institution will need to be upgraded to a supreme audit institution fully independent and functional in line with international standards and EU best practices. Montenegro should also upgrade its Public Internal Financial Control strategy as soon as possible and enhance internal audit capabilities.

4.2.8. *Statistics*

As regards **statistical infrastructure**, the statistical law was adopted by the Montenegrin Parliament. As set out in the statistical law, a statistical council and connected working groups have been established. The positive impact of these changes has not been visible in this period as the aims and objectives of the partners have differed significantly.

A test version of the business register has been developed, but finalisation is slow due to difficulties to obtain uniform data from enterprises.

As regards **classifications** and standards, compliance with EU standards is limited in Montenegro and progress can only be reported for the introduction of the UN classification Custom Tariffs Harmonised System 2002 (HS2002).

As regards the different **sector statistics**, progress can be reported as follows:

For *demographic and social statistics* MONSTAT has published the first results of the harmonised household budget survey (HBS). In the past period, MONSTAT has also made progress in the area of gender statistics by publishing the booklet "Women and Men in Montenegro".

For *macro-economic statistics* MONSTAT has calculated and published the gross domestic product using SNA93 and ESA95 with both production and expenditure approach for the reference year 2003. The calculations for the reference years 2004 and 2005 have also started. In addition, work on the consumer price index has advanced and the first set of figures has been analysed.

For *business statistics* there has been progress in the area of energy statistics and energy balance for electricity has been calculated. For short term statistics and structural business statistics new surveys are being prepared.

For *external trade statistics* the only progress reported is the introduction of the classification HS2002. The production problems from previous periods are still unresolved.

For *transport statistics* the preparation for measuring transport of goods by road has started with the preparation of a questionnaire.

For *statistics on regional level*, no progress can be reported.

For *agriculture and fishery statistics*, the results from the population census of 2003 are being tested to assess the suitability for them being used as a sampling frame. Initial preparations for an agricultural census and fishery statistics have also started.

Regarding management capacity and the development of skills the past period has been dominated by improving the knowledge of basic concepts and of work methods in statistical methodology and sector statistics, whereas initial preparations for other statistical areas were made. MONSTAT staff, including top management, has taken part in training on statistical methodology, languages, organisational theory and statistical software. However, the management capacity and production capacity remain weak and the lack of adequate technical, financial and human resources impairs further progress. As MONSTAT used to rely on assistance from the Statistical Office of Serbia and the Statistical Office of the State Union for producing harmonised statistics, the independence of Montenegro will provide an

additional challenge to MONSTAT. MONSTAT also has to upgrade its capacity regarding international cooperation.

Overall, some progress has been made in the national statistical system of Montenegro in the past period. However, MONSTAT and the rest of the national statistical system need to be substantially enhanced. Development of the administrative capacity, statistical infrastructure and human and financial resources should become a priority in order to deliver timely, reliable and accurate statistics in accordance with EU standards

4.3. Justice, freedom and security

4.3.1. Visa, border control, asylum and migration

Following the independence of Montenegro and the dissolution of the State Union of Serbia and Montenegro, Montenegro has assumed the competences in the area of **visa policy**, which were formerly exercised at the level of the State Union with significant flexibility at the level of the Republics. A draft Law on Aliens is in parliamentary procedure, as well as laws on asylum and citizenship. Pending the adoption of these laws, the Government adopted in June 2006 decisions on the temporary use of travel documents and visas and a decision on a temporary visa regime. The current list of countries for which Montenegro requires a visa for entry to national territory as well as the applied modalities have not been harmonised with the *acquis*.

The Ministry of Foreign Affairs is in the process of building its capacity in this field. Interim solutions have been found concerning the issuing of authorisations to enter Montenegrin territory until Montenegro sets up its own diplomatic missions abroad. Montenegro will have to harmonise its visa policy with the *acquis*. Concerning the issuing of visas it will have to make comprehensive agreements with some other country or countries for representation abroad as the size of the planned Montenegrin diplomatic representations abroad will not allow a substantial coverage of countries whose nationals wish to visit Montenegro. Taking into account that Montenegro is a major tourist destination, a solution to this issue will have to be found as a matter of priority. Strong coordination between visa issuing authorities and border crossing points will have also to be ensured.

Montenegro has announced plans to build up a central citizen registry. The issuance of new travel documents is planned for early 2007, including biometric features. However, legislation on identification cards and travel documents is still lacking.

Concerning **border management**, the Ministry of Interior of Montenegro had already taken over the control of the Montenegrin part of the borders of the State Union in 2003. The institutional strengthening of the border police has continued in particular through training. The reconstruction and equipment of nine border crossings is under way, with EU and donor and budget support. Cross-border cooperation with neighbouring countries is in the process of being upgraded with joint patrols and exchange of information. The legal framework has been completed by the adoption of the Law on the State Border in November 2005. A Strategy on integrated border management (IBM) was adopted in February 2006. Four main bodies (Ministry of Interior, Customs, Veterinary Service, Phyto-sanitary Service) are currently controlling implementation. There is a further need for the adoption of secondary legislation on border crossings management and to establish a coordinating mechanism for integrated border management at national level.

One of the key legislative texts under preparation following the independence of Montenegro is the Law on **Asylum**. Pending its adoption, the Government has pledged that the dissolution of the State Union of Serbia and Montenegro will not have a negative impact on the legal status and protection of refugees and displaced persons currently living in the territory of Montenegro, in particular persons originating from Kosovo. The draft which has been introduced to parliamentary proceedings generally provides for an adequate protection regime for asylum-seekers and refugees, although some provisions remain of concern (exclusion, revocation, judicial review, manifestly unfounded claims, rights and obligations of asylum-seekers and refugees) and will require further elaboration through secondary legislation.

The construction of a reception centre for asylum-seekers and refugees is in progress.

Concerning **migration**, the Montenegrin border authorities prevented 327 illegal border crossings in the period between October 2005 to August 2006.

Fifteen Readmission agreements have been signed, while negotiations on the conclusion of such agreements are ongoing with four further countries. Montenegro has expressed its readiness to conclude a readmission agreement with the Community.

4.3.2. *Money laundering*

Legislation on the fight against money laundering and terrorism financing is in force in Montenegro since March 2005. The list of those obliged to report on suspicious transactions was expanded to include attorneys-at-law and currency exchange offices. Cooperation between relevant agencies continued. The Directorate against Money Laundering operates as a Financial Intelligence Unit. In June 2005, it was admitted as a full member of the "Egmont" Group. A number of bilateral agreements, mainly with neighbouring countries, have been signed. Training is organised for employees of bodies which are obliged to report (e.g. banks). The FIU has signed memoranda on cooperation with law enforcement bodies (Ministry of Justice, Customs, tax administration, Central Bank). As a result, six criminal charges for money laundering were filed in 2005.

However, the Directorate against Money Laundering has not yet developed guidelines on what should be considered as a suspicious transaction and there is no proper monitoring of financial transactions beyond the banking system (especially in relation to real estate and inward investment).

Coordination and exchange of information between the Directorate against Money Laundering and law enforcement bodies as well as tax authorities needs to be substantially upgraded in order to tackle money laundering concerns in Montenegro. Montenegro needs to make efforts to limit cash transactions so that proper controls over suspicious transactions should be exercised.

4.3.3. *Drugs*

Montenegro is faced with huge challenges in relation to drug abuse. Apart from the problems of transit, Montenegro faces also an internal problem of rising drug addiction, with serious social, health and security consequences. Efforts are being made to involve local communities and parents. School policemen have been placed in each school to play a preventive role. Work is also being undertaken regarding rehabilitation.

The National Strategy for Fighting Drug Addiction and the Action Plan for Preventing Drug Addiction among Children and Youth are implemented in line with the EU Drugs Strategy. Legislation on precursors is in force. A multi-disciplinary Commission for Prevention of Drug Addiction among Children and Youth, chaired by the Prime Minister, makes decisions on the realisation and prioritisation of activities and programmes within the Action Plan. Funds are provided out of the Republic's budget. With the view of implementing the Strategy, a Centre for Fighting Drugs and Smuggling has been established within the Police Directorate. This is further supported by seven police units at local security centres. 240 criminal charges have been filed and over 300 kg of drugs seized. While the Centre has responded to international requests for cooperation, further development of international cooperation is essential. There is also a need to improve operational analysis capabilities, including the establishment of relevant database, and to increase intelligence sharing with other countries as well as to improve equipment of the police and customs, in particular at border crossings. Drug-related crimes are the most important single threat, especially in terms of numbers, faced by enforcement bodies. 50% of prison inmates have been convicted for drug-related crimes.

4.3.4. *Police*

The ongoing implementation of the Laws on the Police and the National Security adopted in April 2005 aims at strengthening professionalism, accountability and decentralisation. Specific measures are outlined in the strategic "Vision Document" on police reform from April 2005. A set of implementing by-laws, including the code of conduct for the police have been adopted, and the Department for Internal inspection within the police has been reinforced. The Director of Police has been appointed. There is a need to further strengthen the professional capacity of the police, specialised training, development of intelligence and risk analysis tools. A decree on the Police Academy was adopted in March 2006. The Academy is expected to become operational in September 2006.

The department for the fight against organised crime will need substantial strengthening.

4.3.5. *Fighting organised crime and terrorism*

Organised crime remains a source of serious concern in Montenegro.

Charges have been raised in August 2006 against a criminal group in relation to the murder one year ago of a senior police official who was investigating high-profile organised crime activities, but the case of the murder of the editor and former PM Duško Jovanovic has not been solved yet.

Following the adoption of the Strategy for the Fight against Corruption and Organised Crime, the corresponding Action Plan for its implementation was adopted in August 2006. A Law on Witness Protection has been adopted. A ministerial commission for the implementation of the Witness Protection Programme and Protection Unit have been established. However, no efforts have been made to further develop the legal framework for witness protection in such a way as to ensure that the safety of vulnerable witnesses is appropriately balanced with the right of defence of the accused.

A criminal intelligence system is under preparation. Cooperation with liaison officers is continuously being developed in accordance with the strengthening of crime intelligence. Laws on protection of personal data are under preparation.

Memoranda of cooperation in fighting all forms of crime and terrorism have been signed with Austria, Albania, Bulgaria, UNMIK, Serbia, Croatia and the former Yugoslav Republic of Macedonia, as well as with Italy.

With the appointment of a deputy to the Special Prosecutor charged with the fight against organised crime, the capacity of this office is in the process of being strengthened. Further training and allocation of resources is needed.

Montenegro should cooperate closely with Europol and fulfil the requirements to conclude a strategic agreement with Europol. It should also provide input to the European organised crime threat assessment.

Trafficking in human being represents a serious problem. Montenegro is mainly a country of transit and destination for victims. Efforts and resources to fight trafficking have been increased. The fight against the trafficking of human beings has been strengthened, including the provision of adequate assistance and protection to the victims. A Special Anti-Trafficking Team has been established and has already achieved significant results at the level of police action. However, The Memorandum of Understanding signed between the Government and civil society organisations, for the provision of assistance to victims, has not been fully implemented. The draft Law on Aliens, currently tabled before the Parliament, introduces significant developments in regulating the status of victims – temporary residence for foreign victims of trafficking for a three months reflection period can be extended for a subsequent six months in cases where they participate in criminal proceedings. The provisions on witness protection, under the current legislation, have also been extended to the victims of trafficking in justified cases. In 2005, assistance was provided to 28 victims and to an additional 3 in 2006. The average stay in shelter is about 28 days, while there is a considerable delay in the prosecution of these offences.

The lack of training of judges and prosecutors on trafficking issues affects the efficiency of justice in trafficking cases. Whereas in 2004 and 2005 32 presumed perpetrators have been brought to justice, only four persons have been convicted.

The cooperation between government representatives, international organisations and the civil society has improved assistance to victims,. The further engagement of the government should provide for an enhancement of victim support.

As regards **terrorism**, Montenegro needs to ratify and implement the International Convention on the Fight against Terrorism. The International Convention for the Suppression of Acts of Nuclear Terrorism was signed in September 2005 by the authorities of the former State Union; Montenegro will need to take it over. No cases of terrorism have been registered on the Montenegrin territory.

4.3.6. Protection of personal data

As regards the right to the protection of personal data, the Council of Europe Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data, which is open to non-member states, entered into force in Montenegro in June 2006. However, the Convention is not applied to automated databases containing personal data being kept in accordance with criminal records and state security regulations.

Montenegro has not signed the Additional Protocol to the Council of Europe Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data, regarding supervisory authorities and trans-border data flows.

A Montenegro Law on Personal Data protection has not yet been adopted. The current Law on Personal Data protection of 1998 of the former Federal Republic of Yugoslavia is not in line with the *acquis*. Furthermore, an independent data protection supervisory authority with sufficient powers over the public and private sectors and sufficient means to effectively implement the law is not yet in place.

Therefore current data protection rules are not implemented, and this is a matter of serious concern. Montenegro needs to adopt legislation in line with the *acquis*, in particular with the Data Protection Directive. This is a European Partnership priority and a commitment of Montenegro negotiated under a Stabilisation and Association Agreement.

STATISTICAL ANNEX