



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 5.11.2008  
SEC(2008) 2694

COMMISSION STAFF WORKING DOCUMENT

**CROATIA 2008 PROGRESS REPORT**

*accompanying the*

**COMMUNICATION FROM THE COMMISSION  
TO THE EUROPEAN PARLIAMENT AND THE COUNCIL**

**Enlargement Strategy and Main Challenges 2008-2009**

{COM(2008) 674}

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## STATISTICAL ANNEX

# COMMISSION STAFF WORKING DOCUMENT

## CROATIA 2008 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 report on progress made by Croatia in preparing for EU membership largely follows the same structure as in previous years. The report:

briefly describes the relations between Croatia and the Union;

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

The period covered by this report is from 1 October 2007 to 3 October 2008. 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 Croatia, the Member States, European Parliament reports<sup>1</sup>, and information from various international and non-governmental organisations.

The Commission draws detailed conclusions regarding Croatia in its separate communication on enlargement<sup>2</sup>, based on the technical analysis contained in this report.

#### 1.2. Context

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

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<sup>1</sup> The rapporteur for Croatia is Mr Hannes Swoboda.

<sup>2</sup> Enlargement Strategy and Main Challenges 2008-2009.

### 1.3. Relations between the EU and Croatia

**Accession negotiations** with Croatia have continued. Negotiations have now been opened on 21 out of 35 chapters (*science and research, education and culture, economic and monetary policy, enterprise and industrial policy, customs, intellectual property rights, services, company law, statistics, financial services, financial control, information society and media, consumer and health protection, external relations, financial and budgetary provisions, TENs, transport, energy, free movement of workers, social policy and employment, free movement of goods*) and provisionally closed on four (*science and research, education and culture, enterprise and industrial policy, external relations*).

Of the remaining chapters, discussion continues in Council on seven draft EU negotiating positions (*justice freedom, security, taxation, free movement of capital, CFSP/ESDP, regional policy and coordination of structural instruments and environment, food safety, veterinary and phytosanitary policy*). The Commission is preparing draft EU negotiating positions in three cases (*agriculture and rural development, fisheries and public procurement*).

Based on the overall good progress being made by Croatia, in March 2008 European Commission President Barroso stated that in the 2008 Enlargement package, the Commission would present an **indicative timetable for the technical conclusion of the negotiations** in 2009, provided a number of conditions were met by Croatia. The first condition relates to Croatia meeting all opening benchmarks by June 2008. This is largely done, with the exception of 2 chapters (judiciary and fundamental rights; competition policy) As regards judiciary and fundamental rights, Croatia must make final efforts to meet the outstanding elements of the opening benchmarks. Regarding opening benchmarks for *competition policy*, Croatia must make further efforts, in particular as regards shipbuilding. Secondly, Croatia must comply with all legal obligations under the Stabilisation and Association Agreement (SAA). In this regard, overall compliance is largely assured. Croatia has agreed with the Commission a solution for eliminating the discriminatory taxation of cigarettes. The country needs to pursue efforts as regards the restructuring of shipbuilding. Thirdly, Croatia must continue to comply with the general conditionalities of the Stabilisation and Association Process especially concerning war crimes trials, refugee return issues as well as full cooperation with the International Criminal Tribunal for the former Yugoslavia (ICTY). This has largely been assured. Fourthly Croatia urgently needed to improve its management of EU financial assistance under the PHARE and IPA programmes. Here, good progress was made, which now needs to be translated into concrete progress on the ground (see below). Lastly Croatia must suspend all aspects of the Ecological and Fisheries Protection Zone, with respect to EU vessels. This has been achieved.

The **political and economic dialogue** between the EU and Croatia has continued. Political dialogue meetings were held in Luxembourg in April at ministerial level and in May 2008 in Zagreb at senior official level. Economic dialogue meetings were held in Luxembourg in April at ministerial level and in July 2008 at senior official level. These meetings focused on the main challenges faced by Croatia under the Copenhagen political and economic criteria and reviewed progress being made towards fulfilment of Accession Partnership priorities.

Implementation of the **Stabilisation and Association Agreement (SAA)** has largely continued without major difficulty. The main exceptions have been continued non-compliance with certain state aid provisions, in particular as regards aid granted to the shipbuilding sector, as well as the existence of an excise duty regime for cigarettes incompatible with the SAA. In October, Croatia agreed with the Commission a solution for

eliminating the discriminatory taxation of cigarettes. Previous progress improving implementation of SAA provisions on access to real estate has not been sustained. An Enlargement Protocol to the SAA to take account of the accession of Romania and Bulgaria was signed in July 2008.

The EU provides guidance to the authorities on reform priorities through the **Accession Partnership**. Progress on these reform priorities is encouraged and monitored through the bodies of the SAA. The SAA Association Council met in April 2008 and the SAA Association Committee in December 2007. Seven sectoral sub-committees have been held since November 2007. Based on the Accession Partnership, Croatia adopted its national programme for EU accession in spring 2008.

**Financial assistance** is provided under the new Instrument for Pre-accession Assistance (IPA) from 2007. The 2008 IPA programmes amounted to €146 million. This assistance is concentrated on institution building and preparation for the implementation of the EU's common agricultural policy and cohesion policy. In addition, Croatia continued to benefit from regional and horizontal programmes. Croatia has taken a number of important steps to address weaknesses identified by the Commission in Croatia's management of pre-accession aid. These steps have led to strengthened management and control bodies. A track record of improved implementation is needed.

As regards support to civil society under IPA, a €3 million grant scheme will be launched to support **civil society** projects in the following sectors: transparency and accountability of public administration and fight against corruption, anti discrimination as well as sustainable development. In addition, a €20 million contribution under IPA for cross border cooperation with Italy, Slovenia and Hungary as well as participation in ERDF programmes will promote dialogue between local and regional authorities. Cross border cooperation has also been expanded to Serbia, Montenegro, Bosnia and Herzegovina with a contribution of €4.4 million.

Participation of Croatia in an increasing number of **Community programmes** is also an important tool to implement civil society dialogue.

## **2. POLITICAL CRITERIA**

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

### **2.1. Democracy and the rule of law**

#### *Parliament*

Parliamentary elections were held in November 2007. The elections were free and fair. As regards the electoral roll, some legislative improvements are needed to ensure adequate verification and updating of residence data, which serves as the basis for entry on the electoral roll.

The permanent State Election Commission is now operational at State level. However, adequate staff has not yet been recruited at the local level and further training for all members is needed.

Parliament nominated three new judges to the Constitutional Court. As with previous nominations, the election procedure was held with limited parliamentary and public scrutiny.

The Parliament decided to lift the immunity from prosecution of one MP facing serious criminal charges. It did not, however, agree to lift his immunity from being held in custody. The decision was in contradiction to that of the previous Parliament. This decision was taken despite the seriousness of the charges and the potential effects on witnesses' willingness to testify.

### *Government*

A new government was formed following parliamentary elections in November 2007. The centre-right coalition led by HDZ has a majority of 83 seats out of 153. For the first time the eight minority MPs are official coalition partners and a member of the Serb party, the SDSS, took one of the Deputy Prime Minister posts and became a member of the cabinet.

The Parliament adopted amendments to the ratification of the European Charter on Local Self-Government thereby enabling implementation of the full scope of the Charter.

### *Public administration*

Some progress has been made on public administration reform. The government adopted a Public Administration Reform Strategy for the period 2008 – 2011 as well as a proposal for a revised General Administrative Procedures Act in September 2008. Further implementing legislation for the Law on Civil Service was adopted. The Civil Service law itself was further amended to allow for the planned depoliticisation and to introduce whistleblower protection. A new Administrative Inspection Act was adopted. This Act foresees a higher degree of independence and responsibility of administrative inspectors as well as improved implementation of supervision measures. The number of employees at the Central State Office for Administration (CSOA) increased from 114 to 120. The professional skills and competences of the staff have been improved by various forms of training. In April 2008 the government adopted the 2008 Civil Service Training Plan. Various e-Government initiatives, especially the HITRO.HR (One-stop-shop) project, and the HITROREZ (Regulatory Guillotine) project have been high on the government agenda.

However, the legal basis for building a modern and professional civil service is still incomplete. Major weaknesses in administrative procedures remain and an overhaul of the relevant legislation is still pending. A new salary system is required and the draft Law on Civil Service Salaries has not yet been adopted. The Civil Service Law is not implemented coherently across the state administration due to varying capacities of the relevant departments, the preponderance of agencies and subordinate entities with operational autonomy, and lack of sufficient supervision and follow-up. There is a very limited delegation of decision-making responsibilities from the managerial level to civil servants. The process of de-politicisation of public administration is still at an early stage. Weaknesses in management and administrative capacity of institutions in charge of public administration reform remain. The civil service continues to suffer from high staff turnover and a lack of qualified personnel. There are insufficient capacities for human resources management. Full

effectiveness of various e-government initiatives rely on the correct enforcement of the underlying legal framework, which is neither complete nor properly enforced.

There have been considerable delays in the implementation of Croatia's programme for decentralisation. Currently there is insufficient capacity of public administration at national, regional and local level to manage decentralisation reforms, and to ensure that such reforms actually meet their objectives. The Decentralisation Commission has not become the driving force for the decentralisation process. The local government level is not properly organised and their interest organisation – Association of Towns and Municipalities (SAVEZ) – remains weak.

Overall, some progress has been achieved in the area of public administration reform. However, public administration remains weak and the required reforms continue to represent a major challenge for Croatia. A clear political commitment and further sustained efforts are needed.

#### *Civilian oversight of the security forces*

Reform of the security and intelligence system has continued. The necessary legislation has been adopted and gaps in the existing legal framework have been addressed. With the new legislation adopted, in particular the Law on Security Checks, the intelligence services' conduct and scope of control has improved. However, the legitimate interest of the state to protect certain information and the right of the public to have access to it are not yet properly balanced.

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

#### *Judicial system*

Implementation of the **judicial reform** strategy has continued even if adequate monitoring of its measures has not been possible due to weak administrative capacity. There has been some progress with new legislation such as the adoption of a new misdemeanour Act and a new Act on the seats and jurisdiction of courts, a first step in the court rationalisation process. The system of judicial inspection is starting to show results. A revised Action Plan addressing all major reform issues was adopted in June 2008. However, in certain areas the action plan lacks measurable objectives that will allow effective monitoring of its implementation. While the action plan is a step forward, implementation will be crucial and concrete results are needed. The case backlog remains large and the length of judicial procedures excessive. Court rationalisation has not yet begun in earnest and the current plans lack ambition. Further improvements in the accountability, professionalism and competence of the judiciary are required.

With regard to domestic prosecutions for war crimes, Croatia continues to be active in trying war crimes cases on its own initiative, with around thirty trials in the past year. A more balanced approach is slowly becoming evident with a greater willingness to prosecute perpetrators irrespective of ethnicity. Further progress has been made on regional cooperation on war crimes matters. The State Attorney issued instructions to prosecutors in October 2008 aimed at addressing the problem of a common standard of criminal accountability for war crimes not being applied irrespective of ethnicity. Many such crimes remain unprosecuted, often due to a combination of a lack of evidence, unwillingness of witnesses to come forward, e.g. due to intimidation, and unwillingness or reluctance of police and prosecutors. The issue



of *in absentia* verdicts from the 1990s has not yet been adequately addressed. Limited use is made of the possibility to transfer cases from local to specialised war crimes courts.

Overall, reforms in the judiciary continue but only at a relatively slow pace. Significant challenges remain. Currently, effective dispensation of justice for citizens is not always assured. (*See also chapter 23 - Judiciary & fundamental rights*)

#### *Anti-corruption policy*

There has been some progress in the fight against corruption. The legal framework to combat corruption has been further improved. A revised Anti-Corruption Strategy accompanied by an Action Plan containing specific measures in a number of fields prone to corruption was adopted in June 2008. A new inter-ministerial coordination system for monitoring anti-corruption efforts is in place. The Office for the Fight Against Corruption and Organised Crime, USKOK, continues to become more active and has issued indictments in some important cases. USKOK's role is more widely acknowledged and reports to it of suspected corruption have increased significantly, particularly as regards abuse of office cases.

However, corruption still remains widespread. The administrative capacity of state bodies for fighting corruption continues to be insufficient. The police need to become more effective in the fight against corruption and organised crime. Implementation of anti-corruption efforts has continued to lack strong co-ordination and efficient non-partisan monitoring. While the total number of corruption cases investigated so far has increased, the actual number of prosecutions remains low. There continues to be weaknesses in the work of the National Anti-Corruption Council both in legislative and practical terms. There was little progress in preventing conflicts of interest. The Committee for the Prevention of Conflict of Interest continues to be beset by problems, including the resignation of its chairperson following corruption allegations. A culture of political accountability is lacking. Further efforts are required in tackling high level corruption.

(*See also chapter 23 - Judiciary & fundamental rights*)

## **2.2. Human rights and the protection of minorities**

### *Observance of international human rights law*

As regards **ratification of human rights instruments**, Parliament ratified the Council of Europe Convention on Suppression of Terrorism. The Additional Protocol to the Convention on cybercrime, concerning the criminalisation of acts of a racist and xenophobic nature committed through computer systems, has also been ratified.

Parliament ratified the European Convention on the Compensation of Victims of Violent Crimes. The convention will enter into force at a later date to be determined on the basis of the Law regulating signings and execution of the international treaties.

The **European Court of Human Rights** (ECtHR) delivered 29 judgements in 2007 finding that Croatia had violated the ECHR. As in previous years, the majority of judgements related to the violation of the right to a fair trial and the length of the proceedings under Article 6 of the European Convention of Human Rights (ECHR). The ECtHR found violations of the right to fair hearing in a number of cases in which the local court failed to issue verdicts following previous judgements on violation of this right by the Constitutional Court. The ECtHR court continued to condemn Croatia for violation of Article 3 – inhuman and degrading treatment

concerning prison conditions. A total of 636 new applications to the ECtHR were made during the reporting period. The total number of pending applications before the Court regarding Croatia is 882.

As regards **promotion and enforcement of human rights**, Croatia adopted in November 2007 an Action Plan for the protection and promotion of human rights 2008-2011. Enforcement of rights continued to be negatively affected by shortcomings in the judicial system, however.

Overall, international human rights law is respected in Croatia with some specific shortcomings related to the length of trials and shortcomings of the judicial system.

#### *Civil and Political Rights*

Concerning the **prevention of torture and ill-treatment and fight against impunity**, there has been an increased number of complaints from citizens regarding the excessive use of force by the police. In this context, the Ombudsman has called for more transparent procedures for the determination of police responsibility as well as better regulation of police actions.

A prominent case of forced hospitalisation brought into question the functioning of the police and institutions of the health and social system. The case in question constitutes a serious violation of human rights and illustrates the failure of the system on a number of different levels. Nobody has suffered any consequences to date for the misconduct as identified by the Parliament's human rights committee.

As regards impunity, many war crimes are still unprosecuted, especially those where the victims are of a minority ethnicity (Serbs). In particular in smaller towns there is a lack of will to prosecute these cases.

As regards **access to justice**, Parliament adopted a new Law on Legal Aid in May 2008 aimed at improving the currently limited system. The Law requires a significant build up of the structures for its implementation as well as the adoption of several by-laws. The actual provision of legal aid is foreseen to be available to citizens as of 1 February 2009.

Amendments to the Law on Attorney Service were adopted which envisage Parliamentary control over attorneys' tariffs. Currently tariffs are set independently by the Bar Association and are linked to the length of procedure. These tariffs are too high for the majority of citizens thus preventing their access to the judicial system.

With regard to the **prison system**, first measures have been taken aimed at improving prison conditions, in particular the increase of accommodation capacity. However, there continues to be room for improvement. The lack of capacity has been exacerbated by stricter provisions in the Criminal Code, providing for longer prison terms, and the continued backlog of cases resulting in a longer pre-trial detention.

**Freedom of expression** including freedom and pluralism of the media is provided for in Croatian law and is generally respected. Further progress has been made in following up the recommendations of the 2004 joint expert mission for changes to the laws on electronic media and on Croatian radio and television. (*See also Chapter 10 - Information society and media*)

However, Cases of physical attacks as well as death threats against journalists have gained in prominence and require more thorough investigations. Journalists working on corruption cases or organised crime are increasingly targeted. There has been limited success in identifying and prosecuting perpetrators. Two journalists have been recently murdered. Editors and journalists continue to report undue political pressure. This raises concern about freedom of expression, particularly at the local level.

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

**Civil society organisations** continue to play an important role in the promotion and protection of human rights, democracy and protection of minorities. However, they continue to have difficulty influencing policy debate and remain relatively weak in analytical capacity.

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

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

### *Economic and Social Rights*

As regards **women's rights** and gender equality, implementation of the national policy for the promotion of gender equality continued. Activities to mark 2007 as the year against violence against women, including family violence, continued. In December 2007, a national strategy for protection against domestic violence 2008-2010 was adopted. A new Gender Equality Act was adopted in July 2008. In the new parliament 32 members (21%) out of a total number of 153 are women.

However, there has been an increase in the reported number of acts of family violence. Raised public awareness is one explanation. There has been further improvement in police work in cases of family violence. Centres for social welfare did not show such diligence, however and do not always promptly exercise their legal authority. They also suffer from lack of qualified and trained staff. Croatia remains a country of transit and destination for female victims of trafficking.

Gender equality policy in the field of employment needs more effective implementation, especially as regards access to employment and maternity and child care entitlements. Capacity to cover all reported cases of discrimination in employment needs to be improved. Weakness in the legal system, especially with regard to the length of proceedings, negatively affect the employment rights of women. *See also Chapter 19 – Social policy and employment*

As regards **children's rights**, in October 2007 amendments to the Family Law introduced changes regarding adoption, custody and maintenance for children. The main aim is to reinforce child maintenance in cases of divorce as well as the support to children born out of wedlock. Full implementation will be vital, given the high number of children currently left without financial support.

The Ombudsman for Children continued to play an important role in the overall promotion and protection of children rights in Croatia. The number of individual complaints and general initiatives increased in comparison to 2006 by 63%. This increase is probably the consequence of improved public visibility of the Ombudsman as well as of the opening of three regional offices.

However, the increase in cases has stretched existing resources. Follow-up by line ministries to the inquiries and recommendations from the Ombudsman is in many cases missing. The implementation of measures envisaged under the National Plan of Activities for the rights and interest of children for the period of 2006-2012 has been delayed. The main problems affecting children continue to stem from violence in the family, general parental relations connected to the custody and support of children, but also from weak, understaffed and overburdened social welfare institutions and correctional facilities. There is a general lack of educated experts to provide advice to families. There has been no consolidated approach of the institutions towards the problems regarding child protection issues, including a prevention role of the educational institutions. While the Law on Foster Care strives to improve the quality of foster care, it also brings new restrictions and conditions for fostering that has caused a decline in the number of foster families. Judicial backlogs and lack of trained judges further deteriorate the situation of children, particularly in families at risk of separation or unpaid alimony cases. There is a lack of data on child poverty.

An Act on the Ombudsman for Persons with Disabilities entered into force in January 2008. The first such Ombudsman was appointed by Parliament in May 2008. A National Implementation Plan on Social Inclusion 2007-2008 has been produced. However, continued efforts are needed as regards **socially vulnerable and/ or persons with disabilities**. The relevant legislation is not sufficiently enforced. No tangible progress has been made in the field of de-institutionalisation, including for children with disabilities, even though, with decentralisation, it is among the priorities set out in the Joint Inclusion Memorandum and the related National Implementation Plan. Civil society organisations involved in delivering community based services need to be adequately supported in order to develop sufficiently an alternative to institutionalisation.

With regard to **labour and trade union's rights**, there has been some progress (*See also Chapter 19 – Social policy and employment*). In a difficult socio-economic climate trade unions are playing an increasingly prominent role in public debate. However, workers' rights are still negatively affected by a weak labour inspectorate and a poorly functioning judiciary.

A comprehensive law on **anti-discrimination** was adopted in July 2008, signifying important progress. This law is aimed at full alignment with EU *acquis*. However, anti-discrimination legislation has generally not been applied vigorously. To date there has only been one criminal conviction for hate crime. There has been no conviction for the initiation of racial and other hatred. There has been limited reaction of the authorities to various expressions of an extreme nationalist character which could be considered as incitement to national and religious hatred. There are no statistics on judicial cases to track the nature and extent of discrimination. Support to the victims of discrimination is marginal. The level of protection against discrimination in practice and its judicial prosecution is not in line with EU standards. (*See also Chapter 19 – Social policy and employment*).

**Property rights** are generally assured. However, there are outstanding cases of delayed property repossession and problems with compensation for the use of private property taken under war legislation from the 1990s. The Ombudsman again warned of the lack of proper administrative decisions that should be issued for persons applying for housing care and compensation for the use of their property. Non-issuance of such administrative decisions prevents the claimants pursuing their right to appeal. The process of restitution and compensation for property nationalised after World War II continues to go slowly.

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

### *Minority Rights, Cultural Rights and Protection of Minorities*

Some progress has been made with regard to the implementation of the Constitutional Law on National **Minorities** (CLNM). An Action Plan for implementation of the CLNM was adopted in June 2008 which covers all main issues and relevant institutions. A department for national minorities was established in the Central State Administration Office (CSAO). The CSAO adopted an employment plan for 2008. This plan foresees the recruitment of 158 members of national minorities at the central level and 44 in the offices of the State Administration in the Counties. The capacity of the local councils of national minorities (CNMs) to advise the local government on matters of concern for minorities has improved. Most of the CNMs have been provided with premises and funding. In 2008, the State council for national minorities received around €5.7 million from the state budget for national minority associations. This is an increase of 19% compared to 2007.

However, implementation of the CLNM's provisions in practice presents a mixed picture. Some provisions are implemented well, others only to a limited extent. Problems persist, particularly in terms of under-representation of minorities in state administration, the judiciary and the police. The plan for employment in the administration at County, Town and Municipality level is still not adequate. A long-term strategy to implement the CLNM minority employment provisions is still lacking. Adequate statistics to allow proper monitoring are still missing. No details of implementation of the 2007 targets are available. Despite increased financial support, CNMs are not sufficiently recognised yet as advisory bodies by the majority of local authorities. Moreover, their independence and influence is affected by the fact that they depend on the budget of the town authority or council.

With regard to cultural rights, the education provisions of the CLNM and other laws relevant to minorities are generally being implemented satisfactorily. With regard to the perception of national minorities in the media, negative stereotyping has further decreased. There continues to be little progress with regard to the production and/or broadcasting of programmes for minorities in their languages by public radio and TV stations, as envisaged under the CLNM. Initiatives promoting greater integration, reconciliation and tolerance as well as joint activities within the current system should be further encouraged.

With regard to the Serb minority, there have been some positive developments. For the first time, an ethnic Serb has been appointed to one of the Deputy Prime Minister posts. There have been fewer reports of apparently ethnically motivated attacks against the Serb minority and the Orthodox Church. Police investigations of such incidents have improved, although few cases end in prosecutions. Moreover, a number of ethnically motivated incidents occurred over the summer, which could have a detrimental impact on the willingness of refugees to return. Members of the Serb minority, including those who remained in Croatia during the war, face difficulties concerning access to employment, especially in the war affected areas. Discrimination continues particularly in the public sector at the local level. Croatia needs to encourage a spirit of tolerance and take appropriate measures to protect those who may still be subject to threats or acts of intimidation.

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

More than 2,100 refugees and 1,100 displaced persons returned to their place of origin in Croatia in 2007. The total number of Croatian Serbs registered as returnees to Croatia increased to almost 143,000 although the estimated level of actual return could be less than 60% of this figure. An Action Plan for the accelerated implementation of the Housing Care programmes was adopted in June 2008. Reconstruction of housing has continued. The programme to reconnect public infrastructure in certain return villages is ongoing without major difficulties. Mine clearance operations have continued.

However, a number of obstacles to sustainable return of Serb refugees remain, principal among them being housing, particularly for former tenancy rights holders. Implementation of the Croatian government's housing care programmes within and outside the areas of special state concern (ASSC) for the former tenancy rights holders who wish to return to Croatia continues to be slow, although implementation has picked up in recent months.

Outside the ASSC, only around 530 (12%) of 4,560 requests have been solved definitely. There are a further 1,360 (30%) positive decisions awaiting action. 1,806 are still waiting to be processed (40%) and 864 received a negative decision (19%). The target date for full implementation outside the areas of special state concern has been brought forward to 2009.

Of 8,668 applications inside the ASSC, 4,788 (55%) families have been allocated an apartment out of the 6,816 positive decisions, a slight increase on last year. However, 653 administrative decisions are still pending and 1,199 were decided negatively. For both inside and outside, the negative decisions are under revision, with the help of UNHCR, before they will be sent to the applicants.

The Government's benchmark for 2007 to provide 1,400 accommodation units inside and outside the ASSC has been largely met. For the remaining 60 cases, Croatia has introduced the possibility of daily compensation payments until the foreseen accommodation is available. 598 cases of the 2008 target of 1,400 have been solved.

As regards reconstruction of housing, some 2,700 units were reconstructed in 2007/2008 and approximately 1,500 will be reconstructed in 2008/2009. This will leave an estimated 2,500 housing units still to be reconstructed depending on the outcome of appeals. There remain approximately 8,700 outstanding appeals against negative eligibility decisions, many of which have been pending for four years. Housing assistance has also been extended to applicants with rejected reconstruction claims.

54 houses, of which 45 waiting for a court decision, remain to be repossessed and handed over to their rightful owners. There is still slow progress on repossession of occupied agricultural land. The repair programme for houses damaged or looted prior to repossession is coming to an end.

Apart from housing, other key concerns facing returnees are employment, enduring hostility in certain localities and "convalidation", or the validation of working years concerning pension rights, of those residing in the parts of Croatia not under Croatian government control during the 1990s. In this regard it is positive that the Government has taken various decisions reopening the possibility for these pension rights to be accessed.

The situation of the **Roma** minority in Croatia continues to improve and the administration is developing an increasingly positive and pro-active approach. Some progress is being made on the pre-school education of Roma under the government's action plan for the Decade of Roma Inclusion 2005-2015. Funding is also increasing. The number of Roma children completing primary education and pre-schooling has increased. The issue of lack of legal status of Roma without citizenship is being resolved. For the first time, a member of the Roma minority has been elected to the Croatian Parliament.

However, most Roma remain excluded from mainstream Croatian society and face difficult living conditions. Unemployment remains endemic. Measures with regard to education need to be integrated into more systematic policies. Problems persist also in terms of access to employment, adequate housing, social protection and healthcare, and in general attitudes in society, where discriminatory attitudes prevail towards Roma and other vulnerable groups. Coordination among Roma groups should be enhanced and their expertise for effective implementation should be strengthened. Problems remain regarding the participation of the Roma community in the education system, even when specific programmes are available.

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

*(see also chapter 23 - Judiciary & fundamental rights)*

### **2.3. Regional issues and international obligations**

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

Croatia continues to cooperate with **the International Criminal Tribunal for the former Yugoslavia (ICTY)**. However, there are some problems of access by ICTY to certain documents in Croatia. Croatia needs to ensure a full and proper investigation into the whereabouts of the missing files. The ICTY trial against Gotovina, Cermak and Markac started in March. Before the beginning of the trial, one of the indictees breached on two occasions the conditions of his provisional release. Upon request of the Tribunal, he was arrested and transferred to the ICTY detention centre. The indictee's misconduct triggered the resignation of the Minister of Interior, who had accompanied the indictee on a hunting trip during one of the above mentioned breaches.

An initial verdict was reached in the trial against Rahim Ademi and Mirko Norac, the only **war crimes** case transferred from the ICTY to Croatian jurisdiction. After initial problems where protected witnesses failed to give their testimony, the system of giving testimonies via video link has improved. In May 2008 a conference on regional cooperation in prosecution of war crimes was held with the participation of chief prosecutors from Croatia, Bosnia and Herzegovina, the former Yugoslav Republic of Macedonia, Montenegro and the war crimes prosecutor from Serbia. However, there are still obstacles to the transfer of cases and extradition of suspects in cases of war crimes and crimes against humanity between Bosnia and Herzegovina, Croatia, Montenegro and Serbia. This exacerbates the problem of impunity.

Croatia has not concluded any bilateral immunity agreements granting exemptions from ICC jurisdiction and its policy regarding the **International Criminal Court (ICC)** is aligned with the EU Common Positions on the integrity of the Rome Statute as well as related EU guiding principles.

Some progress has been made with regard to implementation of the **Sarajevo Declaration**, which aimed to finalise the regional refugee return process by the end of 2006. By reopening the possibility for validating pension claims, one of the two main outstanding issues has been tackled by Croatia. Further efforts are needed to resolve the outstanding issues, in particular how to deal with compensation claims of those who lost occupancy and tenancy rights (OTRs) in Croatia.

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

A number of bilateral visits, agreements and continued engagement by Croatia in regional initiatives have contributed towards the aim of further improvement of relations between Croatia and its neighbours.

Croatia has actively participated in the transition from the Stability Pact to a more regionally owned framework with the South East European Cooperation Process (SEECP) and the Regional Cooperation Council (RCC). The RCC Secretariat was formally inaugurated in April. A former State Secretary of the Croatian Ministry of Foreign Affairs was appointed secretary-general. Croatia actively participates also in other regional initiatives such as the Adriatic-Ionian Initiative (chairmanship from June 2007 to May 2008) and the Migration, Asylum and Refugees Regional Initiative (MARRI). Croatia is a party to the Energy Community Treaty and the Central European Free Trade Agreement (CEFTA) and a signatory of the Agreement on the European Common Aviation Area (ECAA).

The application of Croatia's ecological and fishing protection zone (ZERP) also for EU Member States entered into force on 1st January 2008. However, in line with earlier commitments, the Croatian Parliament decided in March 2008 on the suspension of the zone for EU Member States until a common agreement between the countries concerned is found. The Croatian Parliament's decision effectively solves the ZERP issue.

Croatia accepted the *acquis* of the Barcelona process and participated in the launch of the Barcelona Process: Union for the Mediterranean in July 2008, thus becoming a full member of the process.

**Bilateral relations with other enlargement countries and neighbouring member states** continue to develop. There has been some progress towards finding definitive solutions to various open bilateral issues between Croatia and its neighbours, particularly as regards settlement of border disputes.

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

Bilateral relations with *Bosnia and Herzegovina* remain stable. An agreement on police cooperation has been concluded. The Croatian Parliament ratified the bilateral agreement on dual citizenship. There has been no progress on border issues. Ratification of the 2005 Agreement on Demarcation of the Land and River Borders remains on hold. The Peljesac bridge project remains an open political issue. There have been no developments on the agreement on the use of the Port of Ploče. Other unresolved issues include property and refugees.

Regarding relations with *Montenegro*, a working group on outstanding issues, including property, chaired by the ministers of justice has been created and met twice. Agreements on



cooperation in the field of defence and in water management have been signed. Business relations have been enhanced. With regard to the open border issue, the two countries agreed to settle border demarcation at Prevlaka through international arbitration at the International Court of Justice. A joint commission is being established to prepare the legal framework. The temporary border regime in place continues to function smoothly.

Relations with *Serbia* are stable but have been affected by Croatia's decision to recognise Kosovo<sup>3</sup>. The provisional visa-free regime remains in force. There has been some progress in cooperation on missing persons and on war crimes prosecutions. There has been no progress in delimiting the border. Other open matters include property related issues, in particular claims for compensation for lost occupancy and tenancy rights, refugee return, and Croatia's genocide lawsuit before the International Court of Justice, on which hearings began in May 2008.

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

Relations with *Slovenia*, while generally well developed, continue to be affected periodically by difficulties linked to outstanding border issues. Croatia and Slovenia have in principle agreed to involve a third party to resolve the border issue. Joint commissions have been established and held their first meetings. However, there is neither agreement on the body to be entrusted with arbitration nor on the precise subject of final arbitration. There has been no progress in resolving the open issues of Ljubljanska Banka/SFRY Succession Agreement (guarantee of foreign currency deposits). There has been some progress on outstanding issues related to the Krško nuclear power plant, notably through the creation of a special fund by Croatia for future decommissioning costs.

The issue of the non-application of the ecological and fishing protection zone in the Adriatic to EU Member States is resolved.

Croatia has received an invitation to join the North Atlantic Treaty Organisation (NATO), and the Protocol of Accession to the Washington Treaty has been signed.

### **3. ECONOMIC CRITERIA**

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

#### **3.1. The existence of a functioning market economy**

##### *Economic policy essentials*

The country participates in the EU Pre-Accession Fiscal Surveillance procedure. The Pre-accession Economic Programme (PEP) 2008-2010, submitted in December 2007, presents a coherent medium-term framework for economic policies. If fully implemented, it would improve the functioning of markets and support sustainable growth and real convergence. Political consensus on the essentials of market economy has been maintained. However, an

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<sup>3</sup> Under UNSCR 1244/1999

ad-hoc approach to economic policies has often prevailed and a deepening of structural reforms has not figured among the governments' top priorities. The structural reform agenda has moved slowly and there has often been a gap between legislative intent and actual implementation. Policy coordination within the government as well as the government's communication with the Croatian National Bank (CNB) has not been systematically enforced. Overall, consensus on the fundamentals of a market economy has been maintained, but the government's approach to economic policy and reform has sometimes lacked a strategic medium-term orientation.

### *Macroeconomic stability*

In 2007, annual GDP growth showed a marked acceleration to 5.6%, up from 4.8% in 2006, but started to slow in the last quarter of the year. Growth continued to be fuelled by strong domestic demand. Private consumption in 2007 recorded the highest growth rate since 2002 and accelerated strongly to 6.2%, from 3.5% a year before. It remained driven by strong, but slowing credit growth and debt repayments to pensioners, the latter amounting to 1.2% of GDP. The growth of public consumption also increased markedly to 3.4%, to a large extent resulting from pre-election spending increases. Both private and public investment slowed and total investment growth decelerated from 10.9% to a still robust 6.5%. Both the growth of exports and imports declined to 5.7% and 5.8%, respectively, and the contribution of net exports to GDP growth remained negative. On the supply side, the industrial sector added the strongest contribution to growth. Also, the good performance of some services, in particular financial intermediation, retail trade and tourism supported the economic expansion. In the first half of 2008, economic growth decelerated markedly to 3.8% year-on-year, down from 6.8% in the same period a year ago, partly due to slowing exports. At the same time, some rebalancing took place, as consumption moderated amid stronger investment activity. Average per-capita income in 2007 rose to 55% of the EU-27 average<sup>4</sup> from 52% in 2006. Overall, the economic performance remained robust amid some moderation of growth.

The current account deficit continued to widen, from 7.9% of GDP in 2006 to 8.7% in 2007 and to 10.5% in the four quarters to June 2008, mainly due to a rising trade deficit. Relatively strong domestic demand and imports, higher world commodity prices as well as a recent decline in export growth resulted in a widening of the trade gap to 26.3% of GDP<sup>5</sup>. As in previous years, roughly two thirds of the trade gap were covered by the surplus in services, mainly tourism and transport. The deficit in the income balance dropped somewhat due to higher income on equity investments and on foreign exchange reserves. The surplus in transfer payments declined, mainly due to lower government revenues from abroad. In sum, despite strong tourism revenues and higher income from abroad, external deficits have continued to widen, on the back of strong import demand, higher world commodity and energy prices and lower export growth.

FDI remained the main source of foreign financing. In the four quarters to June, the value of net FDI inflows declined by 13.5% year-on-year, representing 7.7% of GDP and thus financing a still large part of the current account deficit. Net inflows were largely driven by the recapitalisation of banks as well as by investments in wholesale trade and the insurance sector, while greenfield investments remained shallow. Owing to continued net capital inflows, official foreign reserves increased to around € 9.3 billion by end-December 2007, and further to € 9.8 billion in August 2008, equivalent to around 5.5 months of total imports.

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<sup>4</sup> In purchasing power standards.

<sup>5</sup> In the 12 months to June 2008

The stock of external debt continued to increase markedly by 14% in the twelve months to August 2008, but the share of short-term debt remained relatively low at 13.2%. The external debt ratio reached 87.8% of GDP at end-2007<sup>6</sup>, up from 85.5% a year before. The share of the domestic banking sector in total external debt declined, as banks reduced their outstanding external obligations during 2007, also in response to central bank measures aimed to contain banks' foreign borrowing. The corporate sector increased its external indebtedness significantly, partly reflecting the circumstance that domestic banks were encouraging their corporate clients to borrow directly from parent banks abroad, thus circumventing their own borrowing restrictions. The increased exposure of the domestic non-tradable corporate sector to foreign borrowing has become a cause for concern and warrants careful monitoring. In sum, capital inflows remained strong and external debt continued to rise, driven by strong foreign borrowing by the corporate sector.

So far, the international financial crisis has only mildly affected the Croatian economy and its financial sector. However, a widening current account deficit and a high level of external indebtedness create important external financing needs requiring significant capital inflows. To that extent, the external imbalances render the Croatian economy vulnerable to possible disruptions in capital flows. The risk of a sudden stop or reversal of capital flows seems limited, but the pace of cross border lending, which has become an important financing source for the domestic corporate sector, could be affected. Higher risk premiums and refinancing costs have already started putting some pressure on the external side. The comfortable foreign exchange reserve position serves as an important cushion in the event of slowing capital inflows. The Croatian authorities lifted the marginal reserve requirement for banks' foreign borrowing to boost their foreign exchange liquidity. Moreover, the deposit insurance law was amended by Parliament, leading a fourfold increase of the guaranteed amount of household deposits (to € 56,000).

Positive trends on the labour market continued. Data from the labour force survey confirm strong employment growth of 2.7% in 2007, which contributed to an increase in the average employment rate to 57.1%, up from 55.6% in 2006. The unemployment rate (ILO) fell from 11.1% in 2006 to 9.6% in 2007. Unemployment declined for all age groups, but still remained high for the young population (at around 24%). The long-term unemployment rate decreased to 5.9% (2006: 6.7%). The officially registered unemployment rate declined to 12.4% in July 2008, compared to 13.7% in July 2007. Labour market developments continued to be characterised by a relatively low job turnover, suggesting rigidities and limited employment restructuring. The growth of average gross wages stayed at 6.2% in 2007, as in 2006, and accelerated to 7.1% in the first half of 2008. Average real wage growth declined, however, due to rising inflation. Overall, the labour market performance continued to improve, but high youth and long-term unemployment and limited job turnover remain a cause for concern.

No major changes occurred with respect to monetary policy. Following the positive experience of previous years in stabilising inflation expectations through a stable exchange rate, the tightly managed float remained in place. Exchange rate stabilisation has also contributed to mitigating significant balance sheet risks under a highly euro-ised financial system. In the last quarter of 2007 and in 2008, the CNB intervened three times in the foreign exchange market and purchased euro for a total amount of around EUR 712 million. Despite a continued surge in capital inflows, the nominal exchange rate of the kuna vis-à-vis the euro

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<sup>6</sup> According to a new reporting system of the CNB, starting in December 2007, the external debt-to-GDP ratio amounted to 88.6% at end-2007.

has been kept stable. The average daily exchange rate fluctuated within a very small range between 7.16 and 7.35 kuna per euro and appreciated by 2.4% in the twelve months to end-September 2008. Overall, the stable exchange rate policy has served the country well and remained a factor of monetary and financial stability.

Reacting to stronger inflationary pressures the CNB gradually increased its marginal repo rate from late 2007 onwards. Moreover, the CNB continued to rely on administrative and prudential measures in order to contain strong capital inflows and rapid credit growth. Marginal reserve requirements on banks' foreign borrowing as well as credit controls remained in place.<sup>7</sup> They were partly adjusted in late 2007 and 2008 to more effectively raise domestic banks' borrowing costs. Partly as a result of these measures, the annual growth of domestic credit to the private sector decelerated from around 23% in 2006 to 15% in 2007 and to 11.2% in August 2008. Both the growth of lending to private households and to the corporate sector dropped. The moderation of lending to the corporate sector, however, also reflects ongoing financial disintermediation of lending, as some corporations turned to direct borrowing from abroad. Overall, in an attempt to contain rapid credit growth, monetary policy continued to rely on administrative measures and credit controls.

Average annual inflation decreased slightly in 2007 to 2.9%, down from 3.2% in 2006. This was due to low carry-over effects from 2006 and low inflation throughout the first half of the year. However, inflation accelerated significantly in the second half of 2007 to 5.8% year-on-year in December, and further to 6.4% in September 2008, compared to 2.1% in December 2006. This acceleration was mainly due to supply shocks linked to considerable increases in the prices of agricultural, food and energy products. Moreover, big increases in administered utility prices, most of which are controlled by local governments, also added to higher inflation. To some extent, increases in household disposable incomes, arising in particular from pension debt repayments and higher government transfers, added to price pressures. There is evidence that rising inflation has led to second-round effects. Core inflation accelerated to 6.5% in August 2008, compared to 3% a year before, and producer price inflation reached one of the highest levels ever recorded (11%). Overall, inflation has increased markedly on the back of higher commodity and energy prices and strong domestic demand.

Fiscal developments in 2007 and in the first half of 2008 benefited from a growing economy and strong revenues, which increased by 13% and 11.5% year-on-year, respectively. Current spending recorded an increase of 10.8% in 2007 and 10.2% in the first half of 2008, fuelled by a strong rise in spending on goods and services as well as on subsidies. In 2007, the general government deficit was reduced as planned, to 1.6% of GDP, down from 2.5% in 2006 (in ESA 95 terms). However, fiscal accounts do not include a number of off-budget operations, such as debt repayments to pensioners (1.2% of GDP in 2007) and quasi-fiscal activities of the State Development Bank (HBOR). Therefore, the actual fiscal policy stance has been more expansionary than the headline budget figures suggest. A revised budget for 2008 was adopted in July and foresees a budget deficit that is slightly lower than originally planned (1.3% instead of 1.6% of GDP), although the main reason for this is the ad-hoc exclusion of the public motorway company from the general government accounts. As in previous years, the revised budget provides for higher than originally projected revenues. They are again used to repay health sector arrears, but also to compensate private households

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<sup>7</sup> However, on 10 October 2008, the central bank revoked the application of the Decision on Marginal Reserve Requirements in an attempt to boost foreign exchange liquidity of the banking sector.

for higher energy prices, and to provide additional funds for regional development as well as for science and education. The stock of general government debt stood at 37.8% of GDP at end-2007, down from 40.8% a year before, and fell further to 34% by June 2008. However, adjustments for the stock of issued State guarantees and the debt of the State Development Bank (HBOR) would raise the stock of debt by around 10 percentage points of GDP. Overall, deficit reduction continued as planned, but actual fiscal policy has been more expansionary than the reported figures suggest. Stronger expenditure restraint remains essential in view of higher inflation and widening external imbalances and as a way to better support monetary policy.

The rationalisation of public spending remained a key public finance objective. The implementation of the social benefits reform strategy adopted in (April) 2007 continued. Its aim is to reduce the number of benefits and to achieve a better targeting of social welfare. However, means- and income-tested benefits as a share of total benefits have remained relatively small while categorical benefits still account for the large majority of social benefits. Although some institutional progress has been made with the establishment of a personal identification number and one-stop shops, the social welfare system remained burdened by complex eligibility criteria and inefficient administration. No new measures have been taken to effectively address the health sector's financial difficulties and arrears continued to accumulate. In particular, the reform of co-payment exemptions through a wider use of means- and income-testing has made little progress. In the context of the 2008 budget revision, the government - as in the previous year - bailed out health sector payments arrears. No measures have been taken to reform the pension system's first pillar. Overall, limited progress has been achieved in terms of increasing the efficiency of public spending.

The government declared itself committed to a comprehensive Treasury Reform Strategy as a sound basis for improving expenditure management and budget control systems. The role of the Ministry of Finance in the budget preparation process has been strengthened. Continued progress was achieved in enhancing institutional and analytical capacity for setting up medium-term macroeconomic and fiscal frameworks. However, public finances still suffer from the absence of a real medium-term expenditure framework which links defined policy priorities to the budget planning process. Some progress has been made in enhancing public debt management capacity, but a fully-fledged strategy is still lacking. Transparency of the issuance policy has remained weak and raises concerns about asymmetric access to information by potential market participants. Efforts were made to reconcile current budget statistics with ESA 95 standards, but important quasi-fiscal operations as well as local governments remained unrecorded, seriously undermining budget transparency. Overall, analytical and institutional capacity in public finance has been further strengthened, but strategy-based budget planning and debt management remained generally weak.

The direction of macroeconomic policies has, on the whole, been appropriate to contain potential external vulnerabilities. Given the limited scope for monetary policy discretion under heavy financial euro-isation, the onus of containing the savings-investment gaps in the economy has remained largely on fiscal policy. Fiscal consolidation has so far benefited markedly from strong revenue growth. However, a credible and sustainable fiscal adjustment process requires much more efforts in accelerating social benefit, health care and pension reforms to bring down the relatively high public spending ratio.

### *Interplay of market forces*

The state continued to gradually withdraw from the productive sector. The sale of 7% of shares of the national oil company INA was successfully completed in late 2007. In June 2008, the government sold 4.2% of Hrvatski Telekom (HT) and 12.5% of a fertilizer company. In all three cases shares were sold to current and former employees. However, the privatisation of assets held by the State Privatisation Fund made only limited progress. A major corruption investigation into the Fund in 2007 led to a de facto suspension of the privatisation process. In early 2008, the government appointed a new head, as well as a new Fund management board, and changed decision making procedures to lend a new impetus to the process. Up until September 2008, the State Privatisation Fund had sold or liquidated some 30 companies and the remaining portfolio still comprised around 891 companies, with the State keeping a majority holding in 97 of them. A number of tenders did not succeed in attracting the interest of potential investors. The private sector's share in output and employment has risen to slightly above or close to 70%, respectively. Overall, progress in privatisation has been uneven and continued to be undermined by institutional weaknesses.

### *Market entry and exit*

Company registration procedures have been further simplified. The average time and number of procedures needed to set up a business, as well as average registration costs, have been reduced further. The number of newly registered companies grew by 1.4%<sup>8</sup> and the stock of active businesses increased by 13% year-on-year in March. An e-register of national regulations has been produced, allowing all regulations to be found in one place. On the other hand, Croatia's performance continues to be relatively unsatisfactory in several measures of the quality of the business environment. Limited progress has been made in advancing the "Regulatory Guillotine" project aimed at simplifying or eliminating regulations that are deemed unnecessary. Doing business in various sectors remained hampered by lengthy and cumbersome procedures for obtaining licences or authorisations at the national and municipal level. Overall, further progress has been made in simplifying company registration, but the business environment continued to suffer from excessive regulations and ad-hoc requirements.

### *Legal system*

Further progress was made in reducing the backlog of cases before Croatian courts. During 2007, the backlog was reduced by 6.1% compared to 2006. However, there is still a large backlog (969,100 cases at end-2007) and the judicial system has remained inefficient. The weaknesses of the judicial system may discourage economic actors from taking cases to court and undermine effective enforcement of creditor and property rights.

### *Development of the financial sector*

The financial sector, still dominated by banks, represented around three quarters of total assets at end-2007. Some 95% of banks are privately owned and the share of foreign ownership remained high at 90%. The number of banks was unchanged at 33, which is relatively high in relation to the market size. The degree of market concentration has remained at a moderate level and has generally not been an impediment to market competition. The five largest banks

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<sup>8</sup> Last quarter 2007 and first quarter 2008 compared to same period a year before

together accounted for a market share of around 68% at the end of 2007, down from 72% in 2006. The spread between the weighted average of new kuna-denominated loans and new kuna-denominated deposits did not change significantly. Domestic private credit rose to 73% of GDP in 2007, up from 69% in 2006. Overall, the largely private and foreign-owned banking sector remained the key player in financial intermediation.

The banking sector has become more resilient as a result of a number of prudential and supervisory measures that have been taken to address potential macro-financial vulnerabilities. Additional capital requirements were imposed on fast-growing banks, and risk weights on un-hedged foreign currency loans were increased. Banks' capital adequacy, asset quality and profitability remained at comfortable levels. The share of non-performing assets remained at a relatively low level of 3.2% in June 2008, although this indicator may underestimate portfolio risks during periods of strong asset growth. However, the banking system still has to contend with interest and exchange rate induced credit risks, as the majority of loans are based on variable interest rates and linked to foreign exchange. Very good progress has been made in the central bank in fostering the analytical capacity to produce forward-looking financial sector stability assessments. Overall, additional prudential measures served to make a generally sound banking system even more resilient and reduced potential macro-financial risks.

The share of non-banking financial sector assets in total financial sector assets increased from 23.4% at end-2006 to 26 % by end-2007, also due to the strong asset growth of investment funds and mandatory pension funds. In 2007, domestic stock markets generally benefited from the strong growth of non-bank institutional investors and increased interest from the general public in equity investments, although the turnover remained low. This resulted in a strong increase in the stock market index by 60%, taking market capitalisation to around 128% of GDP at end-2007, as against 79% in 2006. Since the start of the year, the Croatian stock market has been rather volatile and the Zagreb stock exchange index lost around 50% in the first ten months. Market capitalisation had declined to 90% of GDP in June 2008. Bond market capitalisation amounted to 13% of GDP in June 2008, slightly lower than a year before, as the market capitalisation of the corporate sector declined. The supervision and regulation of the non-banking financial sector has gradually improved. The previously unregulated leasing sector has been brought under the oversight of the non-bank supervisor HANFA. Also, HANFA and the Croatian stock exchange have adopted the Croatian Corporate Governance Codex, which, if properly applied, should enhance the transparency and efficiency of the capital market. In general, notwithstanding the growth of some market segments, capital markets remained shallow, with little turnover.

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

#### *Existence of a functioning market economy*

Macroeconomic stability has been largely maintained and has allowed economic agents to make decisions in a climate of stability and predictability, thus supporting the functioning of market mechanisms. However, significant state interventions in the economy as evidenced by a high spending ratio and high subsidies, as well as prevailing obstacles to private sector development, continued to partly undermine a more growth-oriented allocation of resources, constraining the potential for higher productivity and catching-up.

### *Human and physical capital*

Reforms in the education sector have continued under the Education System Development Plan for 2005-2010. Further steps were taken to improve the quality of education at all levels. A national programme aims to increase the rate of enrolment in and completion of secondary education and to reduce the percentage of early school leavers. However, the education sector continued to suffer from out-dated curricula and poor equipment. The joint assessment of employment priorities was signed by the Commission and the Croatian authorities. The government continued to implement active labour market policies. These include training and employment subsidies for young people without work experience, the long-term unemployed, older persons and vulnerable groups. However, although there was a slight increase in employment and participation rates, the levels remained relatively low - at 57% and 63.2% respectively in 2007. Overall, the labour market continued to suffer from mismatches between supply and demand.

Investment continued to be robust in 2007 and 2008, albeit growing at a slower pace, and the fixed investment ratio remained high at around 30% of GDP in 2007. Total spending on research and development remained at the relatively high level of around 0.9% of GDP. Public investment in transport remained strong. In particular, investments in new highways amounted to 1.9% of GDP and resulted in a further expansion of the network. Most of the core main lines of the rail network are sufficiently well maintained to allow a competitive freight transport business. FDI continued to play a significant role. The total stock of FDI reached EUR 17.6 billion (47% of GDP). The largest share of cumulative FDI inflows is accounted for by the financial sector (36%), followed by manufacturing (27%), and post and telecommunications (10%). There has still been little greenfield investment, and private investments in the processing and manufacturing industry have remained relatively low, limiting technological change and export potential. To conclude, strong levels of investment continued to be concentrated in transport infrastructure and the services sector.

### *Sector and enterprise structure*

The loss-making, state-owned aluminium company (TLM) was sold following lengthy tender procedures and negotiations. Subsequently, the new owner submitted a restructuring programme to the government. Following the privatisation of the two steel mills, the government adopted a revised National Restructuring Plan for the steel industry. In the area of shipbuilding, the government adopted revised individual restructuring plans, as well as taking a decision to restructure six shipyards through a process of privatisation. The privatisation process is expected to start immediately and to be completed by the end of 2009. However, details concerning methods and conditions for sale have not yet been agreed. Overall, there has been mixed progress with the restructuring of large loss-making companies.

The restructuring of the loss-making large railway carrier has made very limited progress. The objectives of the business plan for 2007, in particular significant staff reductions and a wage freeze, were not met. The envisaged reduction of the working ratio in 2007 did not materialise, and the ratio even started to worsen in 2008. The railway sector continued to require high levels of budget support (above 1% of GDP in 2007). Low productivity and high unit labour costs continue to undermine its long-term viability, necessitating vigorous action, including staff lay-offs and the closure of non-profitable lines. Four railway subsidiaries were tendered for privatisation, but have not yet been sold. The liberalisation of the telecommunication industry continued. The Croatian Telecommunications Agency continued with activities aimed to stimulate market competition by improving market access to new



service providers. This led to further price reductions and to a larger choice of tariff packages for customers. New fixed line competitors raised their market share further from 13% to a still modest 19%, but the incumbent Croatian Telecom remained by far the dominant operator. The liberalisation of the energy sector continued to advance gradually with the opening of the electricity market to private households as of 1 July 2008. While this marks an important formal step towards more competition, the large public energy company HEP remained de facto the only energy supplier. Moreover, the restructuring of HEP has not seen any progress. Overall, the reform of network industries made headway, but the railway sector needs much deeper restructuring in order to ensure its long-term viability and competitiveness.

The already large service sector increased its share of total output to 63%. Agriculture's share of output declined further to 6.8% in 2007. The share of construction and industry together accounting for around 32%, remained unchanged. Agriculture's declining share of employment fell to 13%, while industry and construction rose to above 30% and the services sector maintained its share of around 56%. Given the already large service sector, there were only marginal shifts in the sector structure of the economy.

The small and medium-sized enterprise (SME) sector continued to grow in 2007, representing more than 40% of the corporate sector's total assets, 66.2% of total employment and 65% in total investment. SMEs generated more than 45% of GDP and accounted for an increasing share (above 40%) of total exports. The government decided to extend the existing support schemes for SMEs by adopting a new medium-term programme (2008-2012). However, the sector continued to suffer from a cumbersome regulatory framework and inefficiencies in public administration. Access to longer-term financing remained difficult, particularly for newly established businesses. Overall, the SME sector has gained in importance, despite the remaining administrative obstacles.

#### *State influence on competitiveness*

The government has taken short-term measures to alleviate the impact of higher energy prices on households, such as increasing income tax allowances and granting subsidies to the electricity company. However, as price subsidies are linked to the level of consumption, it remains doubtful whether these measures will be effective in targeting the most vulnerable parts of the population. Also, they may risk distorting necessary price signals. The role of the Competition Agency in monitoring and controlling State aid has been further strengthened, but the relatively low staffing levels continued to be an urgent problem. The total amount of subsidies in the 2007 and 2008 general government budgets remained high - at 2.6% of GDP - and a large share has still been provided to loss-making companies. Horizontal aid accounts for only a small share of total subsidies. Overall, state intervention in the enterprise sector remained substantial.

#### *Economic integration with the EU*

Croatia is an open economy with total trade in goods and services representing more than 100% of GDP. Apart from the export of transport equipment (mainly ships), tourism continued to be the biggest source of export revenue, representing almost 18% of GDP in 2007. The EU has continued to be the most important trading partner, although its share in total Croatian exports and imports fell by a few percentage points to 60.9% and 64.8%, respectively. At the same time, Croatia has expanded its trade with neighbouring countries, also reflecting ongoing regional trade integration. Around 97% of FDI inflows originate from

EU Member States. Overall, integration with the EU in the areas of trade and investment remained very high, and trade with neighbouring countries has continued to grow.

The average growth in real wages stood at around 3% in 2007, and remained in line with estimated changes in average labour productivity, with the result that real unit labour costs remained largely unchanged. The nominal effective exchange rate of the kuna appreciated by 3.2% as a result of strong upward movement against the US dollar. In real effective terms<sup>9</sup>, the kuna appreciated at a somewhat higher rate (3.8%), reflecting a slightly faster growth of domestic producer prices relative to producer prices abroad. Overall, standard indicators do not point to significant changes in export price competitiveness.

#### 4. ABILITY TO ASSUME THE OBLIGATIONS OF MEMBERSHIP

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

##### 4.1. Chapter 1: Free movement of goods

Good progress can be reported regarding alignment on **general principles**. Croatia adopted in November 2007 an Action Plan for compliance with Articles 28 to 30 of the EC Treaty, which defines specific tasks for compliance, sets up target dates for national and local authorities, and defines the necessary institutional structures to enable the removal of all measures having an equivalent effect to quantitative restrictions on imports and exports. This was a key element in the accession negotiations on this chapter.

Good progress can also be reported in the area of **horizontal measures**. Key horizontal legislation and the Strategy for the implementation of the *acquis* in the field of free movement of goods were adopted in November 2007. The Strategy provides for a comprehensive framework for effective implementation of EC legislation, complemented by realistic milestones and measures to enhance administrative capacities. Nevertheless, particularly the Law on Technical Requirements for Products and on Conformity Assessment and other relevant horizontal legislation still need further alignment with the *acquis*, especially with the new framework *acquis* relating to the marketing of products.

As regards *standardisation*, by the end of August 2008 the Croatian Standards Institute (HZN) had transposed 10,695 harmonised European standards. The number of HZN staff has increased to 61 as of September 2008. HZN is an affiliate member of the European Committee for Standardisation (CEN) and the European Committee for Electrotechnical Standardisation (CENELEC). Further efforts are needed on the part of HZN to ensure the timely adoption of its strategies and action plans, as well as European standards, in order to complete the preparations for CEN/CENELEC membership by December 2008. The reorganisation of the infrastructure of the technical committees is underway with 154 restructured committees as of end-August.

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<sup>9</sup> As measured on the basis of producer prices

Concerning *conformity assessment*, the ordinance on the form, content and graphic symbol of the conformity marking (CE) for products confirming compliance with the prescribed technical requirements entered into force in May 2008.

In the area of *accreditation*, the Croatian Accreditation Agency (HAA) has in July 2008 adopted its development strategy for 2008 – 2010. It has continued to promote accreditation among governmental institutions responsible for harmonisation under the new and old approach *acquis*. By August 2008 HAA had accredited a total of 123 conformity assessment bodies. HAA has 22 permanent employees, 59 lead assessors (HAA employees and external associates), 88 technical assessors (mostly external associates) and 117 experts (external associates). European Co-operation for Accreditation (ECA) has started a pre-evaluation process in June 2008 for granting the signatory status of its multilateral agreement to HAA.

As regards *metrology*, the National Strategy in the field of metrology (2007-2013) was adopted at government level in May 2008. This lays the foundation for the setting up of the new metrology infrastructure, including the National Metrology Institute, and for financing its development. A regulation on the establishment of the institute has been passed in June 2008, and preparations for its setting-up have started.

Regarding *market surveillance*, there is some progress to report with regard to the State Inspectorate's administrative capacity and enforcement measures. The Regulation on the internal organisation of the State Inspectorate was amended in December 2007. This reform allows recruitment of new market inspectors. It also introduced new departments, such as the Department for European Integration, and expanded the scope of work of others, such as the Departments for Conformity Testing and for Consumer Protection. Within the latter department, two new sections were created: the Section for the Control of the Sale of Products and Supply of Services, and the Section for Products Notification and Information Exchange (Rapid alert system for non-food products - RAPEX), for which the National Contact Point was established. Guidelines for the control of the trade in and labelling of textiles and footwear and guidelines for the placing on the market of personal protective equipment have also been produced.

In terms of administrative capacity in the Ministry of Economy, Labour and Entrepreneurship (MELE), there has been progress in the Department for Internal Market Coordination. The department is responsible for alignment and implementation of technical legislation, overall policy coordination with other ministries and agencies and for the application of Articles 28 to 30 of the EC Treaty. In the first quarter of 2008 the new organisation of the Department was adopted and the number of staff was increased to 20.

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

There has been some progress in sectors covered by the **old approach** *acquis*, most notably in the field of motor vehicles, textiles and medicinal products for human use and veterinary medicinal products. Two Ordinances, on the pricing of medicinal products and on the criteria for including products on the list of medicines respectively, were adopted in June 2008. However, they seem to need amending to be fully compatible with the *acquis*. Further efforts are needed in order to reach full legislative alignment and necessary administrative capacity, particularly with regard to pharmaceuticals, chemicals, cosmetics and motor vehicles.

Although the legislative alignment with the **new and global approach** *acquis* has been advancing, many of the national alignment measures have still to be verified. Further efforts are still needed, particularly with regard to low voltage equipment, toys, machinery, equipment and protective systems intended for use in potentially explosive atmospheres, construction products, gas appliances, pressure equipment and simple pressure vessels, cableway installations, noise emissions by outdoors equipment, emissions of pollutants from non-road mobile machinery engines, and eco-design requirements for energy-using products.

As regards **procedural measures**, there is some progress to report. In June 2008, Croatia adopted a Regulation laying down procedures for the provision on notification in the field of standards, technical regulations and conformity assessment procedures and of regulations on information society services which aims at transposing Directive 98/34/EC as amended by Directive 98/48/EC. Secondary legislation has been adopted as regards acquisition and possession of weapons.

### *Conclusion*

Good progress has been made on alignment of legislation with the *acquis* on free movement of goods. Although alignment with the *acquis* in this chapter is well underway, some elements are not yet in place. Adjusting the conformity assessment infrastructure and market surveillance activities remains a major challenge. Croatia needs to make considerable efforts and continue the process of alignment with the *acquis* and its effective implementation and enforcement, and develop before accession, policies and instruments that are as close as possible to those of the EU.

## **4.2. Chapter 2: Freedom of movement for workers**

Some progress has been made in the area of **access to the labour market**. Amendments to the Act on Pension Insurance Companies and the Payment of Pensions Based on Individualised Capital Savings were adopted in October 2007 aiming at enabling cross-border payment of pension benefits in the supplementary pension scheme.

Some progress can be reported on future participation in the **EURES** network. Amendments to the Act on Employment Mediation and Unemployment Rights were adopted in July 2008 aiming at ensuring equal treatment of EU migrant workers and Croatian citizens as regards assistance by the national employment office. The organisational structure of the Croatian Employment Service is being adjusted and administrative capacity strengthened as regards services related to mobility and free movement of labour. Gaps remain in the language skills of potential EURES advisers and, with a view to the required connection to the EURES Job Mobility Portal upon accession, in ensuring that all job vacancies of the Public employment services are displayed on its public website and can therefore be made available for publication on the Portal. In this area, Croatia is already moderately advanced.

There has been no significant progress on **co-ordination of social security systems**. Sufficient administrative capacity has not yet been developed to apply the *acquis* in this field.

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

## Conclusion

Some progress has been made on this chapter. A satisfactory level of legal alignment has been reached. However, Croatia's legislation is not yet in line with the EU rules on access to the labour market. Sustained efforts are also needed to develop the necessary administrative capacity, notably for the co-ordination of social security systems, which is a key element for the accession negotiations in this chapter.

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

Limited progress can be reported on the **right of establishment**. The new Veterinary Act adopted in 2007 removed certain restrictions, such as a requirement to hold Croatian citizenship in order to exercise in private practice, and will apply with effect from the date of accession. The Law on pre-school education was amended in order to remove the distinction between Croatian and foreign physical and legal entities for the purpose of authorisation to set up kindergartens in Croatia. Under the amended Law on institutions, with effect from the date of Croatia's accession to the EU, Croatian and foreign legal and physical persons will have equal right of establishment of institutions.

Numerous restrictions on the right of establishment still exist in many sectors, in the form of citizenship, residence and disproportionate language requirements, plus a mandatory minimum duration (six months uninterrupted) for certain economic activities and the one-office rule.

There has been some progress regarding the **freedom to provide cross-border services**. The amendments to the Company Law (which were adopted in October 2007 and entered into force in April 2008) introduced a distinction between provision of services on a temporary basis and permanent establishment, hence making it possible for foreign entrepreneurs to provide cross-border services without establishing a branch office. Cross-border company mergers have been regulated, but the amendments will not become applicable until the date of accession. However, several restrictions that hamper cross-border provision of services remain in both general and sectoral acts. The amendments to the Act on physical planning and construction introduced some potentially discriminatory measures as regards EU companies.

Some progress has been made in the field of **postal services**, where the level of legislative alignment is already relatively high. The Strategy for Postal Services Market Development in the Republic of Croatia and the Action Plan for implementation of the Strategy were adopted in March 2008. The Strategy proposes a timeframe for further liberalisation of the postal services market in Croatia. The amendments to the Postal Act, which entered into force in July 2008, strengthened the supervisory power of the regulatory body. With the adoption of the Law on Electronic Communications the Council for Postal Services was merged together with the Croatian Agency for Telecommunications into single Agency for Post and Electronic Communications. The tasks and objectives regarding the regulation of postal sector in Croatia did not change with this transformation. Provisions on further liberalisation of the postal market will not enter into force until 1 January 2010, when the price limits and reduced reserved area for items of correspondence up to 50 g will be in line with the EU *acquis*. According to the above mentioned Strategy it is envisaged that the postal market would be fully liberalized by the end of 2012. However, the exclusive rights in the postal sector in Croatia are broader than provided for in the *acquis* and there is not yet any possibility for a natural person to apply for a licence.

Some progress has been made on **mutual recognition of professional qualifications**, but improvement still needs to be made. The Legal Profession Act was amended in September 2008, aligning with the *acquis* by allowing upon accession EU lawyers to provide legal services and to dispense legal counsel in Croatia, including in the form of law firms, and to establish subsidiaries. A new law has been adopted with the aim to align with commercial agents' directive. The minimum training requirements for the medical professions (doctors, dentists, midwives, nurses, pharmacists) are still not in line with the *acquis*. As regards dentists, the professional and academic title ("stomatology") used is not recognised under the *acquis*. The nurses training at secondary and higher school level, the midwifery secondary level education and the in-service training at the 5<sup>th</sup> year for pharmacists, all fall short of the requirements set out in Directive 2005/36/EC. Legal or administrative provisions laying down the minimum training requirements to be respected by all training institutions are still missing.

In September 2008, amendments to several acts in the health sector were adopted to waive Croatian citizenship requirements and to bring language requirements in line with the *acquis*. These changes will be applicable as of the accession date. The administrative capacity of the authorities dealing both with mutual recognition of qualifications and with coordination and alignment with the *acquis* as regards freedom to provide services needs to be strengthened. However, the preparations in the field of mutual recognition of professional qualifications are well on track.

### *Conclusion*

Some progress has been made on this chapter, notably on the right of establishment and freedom to provide cross-border services. However, further substantial work is required in order to align Croatia's legislation fully with the *acquis* in this chapter, as various obstacles to the right of establishment and freedom to provide services remain in both the general and the sectoral legislation. Overall, alignment with the *acquis* is at a reasonable level, although considerable efforts are still required in some areas. Strengthening of the related administrative capacity is required.

## **4.4. Chapter 4: Free movement of capital**

Some progress can be reported concerning **capital movements**. As regards real estate, the administrative capacity of the Ministry of Justice was reinforced in order to expedite the processing of applications from foreigners for permission to purchase. This has resulted in a substantial reduction of the backlog of pending requests from EU nationals. Procedures have been speeded up for all applicants, applications have been processed on a non-discriminatory basis and transparency of the process has improved. However, in recent months a slowdown in the processing of applications was noted. As regards other capital movements, some discriminatory provisions still remain in Croatian legislation, in particular concerning institutional investors, including "golden shares", and the use of assets in building societies. Clauses that are not in line with the *acquis* have even been introduced in privatisation contracts concluded during the reporting period.

There has been some progress in the area of payment systems. External payment operations were further liberalised by allowing residents to freely accept payments from non-residents and to allow payments to non-residents in domestic currency without any limitations. The rules on statistical reporting of credit transactions with non-residents were modified in order to remove capital restrictions.

As regards **anti-money laundering** (AML), the Croatian government adopted a comprehensive action plan aimed at reinforcing the legal and institutional framework. A new AML law was adopted in July 2008 and will enter into force in January 2009. It constitutes a major step forward in strengthening Croatia's AML regime by aligning it substantially with the *acquis* and Financial Action Task Force recommendations. Some marginal amendments to the AML legislation will be necessary to achieve full alignment. Croatia ratified the Council of Europe Convention on Laundering, Search, Seizure and confiscation of the proceeds of crime and on financing of terrorism. However, institutional capacity needs to be strengthened. Monitoring and supervision of reporting entities remains inadequate, especially outside the banking sector, and the enforcement record (including convictions, confiscations, seizures and asset freezing) is still weak. Moreover, further efforts are required in improving anti-money laundering legislation, ensuring effective implementation, strengthening the FIU and improving inter-agency cooperation.

### *Conclusion*

There has been some progress in this chapter, mainly as regards the processing of applications for permission to acquire real estate by EU nationals and the adoption of an action plan and new legislation in the area of anti-money laundering. Overall a reasonable level of alignment has been achieved, although further efforts will be needed especially with implementation and enforcement.

## **4.5. Chapter 5: Public procurement**

Good progress can be reported in the area of improving the overall public procurement system, including **general principles** deriving from the Treaty. The new Public Procurement Act entered into force in January 2008. This law brought Croatian legislation further in line with the *acquis* in terms of the award of public contract and remedies. Implementing regulations were also adopted. Further amendments to the Public Procurement (PP) Act were adopted in October. A New Concessions Act was also adopted. In June 2008 the Government of Croatia adopted a Comprehensive strategy on the development of the public procurement system (including concessions and Public Private Partnerships) and an Action Plan outlining a clear timeframe for each of the actions needed for public procurement reform, which is being implemented according to its timeframe.

As regards **award of public contracts**, E-procurement regulations and their implementation require further development in order to increase the transparency and efficiency of public procurement. The level of knowledge of Public Procurement legislation remains low and further development of administrative capacity is required both at central and local level. In particular the procuring entities do not have enough knowledge of the legislation and of the procurement procedures. However the strategy adopted in June 2008 includes a comprehensive training programme including all involved stakeholders.

Besides the relevant parts under the Public Procurement Act there has been no further development on legislative alignment in the area of **remedies**. The competence of the State Commission for the Supervision of Public Procurement Procedures does not yet cover remedies on concessions. The State Commission has established a good reputation over the last years. It has made some necessary staff recruitments during the past 12 months and shows a good track record in solving cases. To increase transparency all decisions of the State Commission have been published on its web-site since April 2008.

Regarding *administrative capacity* a government decision of March 2008 tasked the Ministry of Economy, Labour and Entrepreneurship (MELE) with the responsibility for coherent policy making, coordination and implementation of the public procurement system. In MELE, the Directorate for Public Procurement System has been set up to replace the former Public Procurement Office. In order to ensure coherence, MELE closely cooperates, both on political and technical level, with other stakeholders of the procurement system: Ministry of Finance (concessions), PPP Sector at the Trade and Investment Promotion Agency (TIPA) (implementation of PPP projects) and State Commission for the Supervision of Public Procurement Procedures (independent review body). Since the government decision, all the affected state authorities (MELE, Ministry of Finance, State Commission, TIPA) have increased their staff.

### *Conclusion*

Good progress can be reported in this chapter in particular in terms of establishing the necessary institutional set-up capable of managing the public procurement policy and in terms of a adoption of a comprehensive strategy. However, further legislative alignment is needed and administrative capacity remains to be improved at all levels of the procurement system. Emphasis should now be put on the proper and effective implementation of the new Public Procurement Act. Anti-corruption measures also need to be embedded at all levels of the system covering both the legal framework and its functional application ensuring greater transparency and efficiency.

## **4.6. Chapter 6: Company law**

Further progress has been recorded in the field of **company law**, where Croatian legislation is largely aligned with the *acquis*. The Act on Amendments to the Companies Act entered into force in April 2008 except for the provisions of Article 142, which will enter into force on the date of accession of Croatia to the EU. The Court Register Act was amended at the same time in order to be in line with the provisions of the First Company Law Directive. A new application connecting court registries into a single database of registered entities has been operational since April 2008.

The Bankruptcy Act, the Act on the Introduction of the *Societas Europea* (SE) and European Economic Interest Group (EEIG) were enacted in October 2007 and will come into force as of the day of accession. An alignment with Council Directive 2001/86/EC supplementing the Statute for a European Company with regard to the involvement of employees is still outstanding.

The Act on Takeover of Joint Stock Companies was published in October 2007 and ensures the implementations of the provisions of the 13<sup>th</sup> Company Law Directive.

There has been good progress in the field of **corporate accounting**. The new Accounting Act, which had been adopted in October 2007, entered into force in January 2008. The provisions regulating the application of the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS) and the provisions regulating audit of annual financial reports (mandatory for all large and medium-sized enterprises and all other listed companies or companies that are prepared to be listed) will be applicable as of Croatia's accession to the EU. In March 2008 the new Croatian Financial Reporting Standards were adopted. Ordinances on the layout and content of annual accounts and on register of new



accounts were also adopted). Overall, the level of approximation with the *acquis* in the area of accounting seems satisfactory.

The Tax Administration as the institution in charge for enforcement of the new accounting Law received some training. However, the number of staff remained unchanged.

There has been limited progress in the field of **auditing**. Work on the new Audit Act is at the final stage. The Chamber of Auditors needs further strengthening to be able to ensure proper implementation of financial reporting standards.

### *Conclusion*

Overall, some progress can be reported in this chapter. Alignment with the *acquis* in the area of company law is on track, but continued efforts are required for implementation of the recently adopted amendments regulating accounting and strengthening of administrative capacity.

## **4.7. Chapter 7: Intellectual property law**

There has been good progress in the field of **copyright and neighbouring rights**. In January 2008 Croatia became a full member of the European Patent Office (EPO). An interpretative statement on collective rights management societies has been adopted, thus providing for further alignment with the EU *acquis*.

The amendments to the Civil Procedure Act shortened civil procedures. Croatia still needs to align its criminal procedural law with the Convention on cyber-crime concerning copyright and related rights. There has been some progress on **industrial property rights**, as implementing legislation was adopted to complete the legislative framework. Minor changes to legislation on patent, trade marks and topographies of semiconductors are still needed to achieve full alignment with the *acquis*.

Good progress can be reported on **enforcement**. The State Intellectual Property Office (SIPO) has developed the methodology for collection of statistical data on enforcement, which will be used for the annual reporting. In comparison with the previous reporting period, there was a significant increase in the number of misdemeanour proceedings launched in response to investigations by the State Inspectorate. The Board of Appeal within SIPO was appointed in June 2008. Although numerous workshops and seminars on protection of intellectual property rights have been held for judges and State attorneys, further specialised training for the judiciary and overall awareness raising is still needed.

As regards administrative capacity, guidelines for applicants were published by SIPO and an information centre (INCENTIV) was opened in January 2008. Esp@cenet – an on-line searchable patent, trademark and industrial design database available to the public – was completed in April 2008. As regards inter-institutional cooperation, the Customs Agency started to notify the Ministry of Justice and the State Inspectorate regularly in the event of reasonable suspicion of IPR infringements related to goods subject to customs procedures. However, further efforts are needed to improve cooperation between all authorities engaged in IPR enforcement.

## *Conclusion*

Good progress can be reported both on legislative alignment and on enforcement. Alignment with the *acquis* is at a very high level. However, some minor changes are still needed. Further efforts are required to strengthen the administrative capacity for enforcement of IP rights and, especially, to raise awareness amongst stakeholders. Continued attention has to be paid to the fight against piracy and counterfeit goods.

### **4.8. Chapter 8: Competition policy**

There has been no further alignment of Croatian legislation with the *acquis* in the field of **anti-trust** including **mergers**.

As regards administrative capacity, in 2008 15 economists and lawyers out of 45 employees of the Croatian Competition Agency (CCA) were dealing with competition cases. Although new personnel have been employed, there have also been staff losses. There is a need to increase CCA administrative capacity.

In the course of 2007 the CCA brought 56 substantial decisions in the field of antitrust and mergers and in the first quarter of 2008 9 decisions were brought. . Of these there were 25 concentration cases, 24 of which were approved unconditionally. One concentration was conditionally approved in the retail and press distribution sector. In addition, one prohibited agreement was identified in the bus transport sector. Two cases of abuse of dominant position were confirmed in telecommunications and press distribution markets. In both abuse cases the remedies imposed by the CCA were fulfilled by the undertakings within the given deadlines. In addition, the CCA has dealt with 27 cases pertaining to the promotion of the culture of competition. In the first quarter of 2008 another 9 substantial decisions were adopted, seven of which concerned mergers that were approved in the first phase. In the second quarter of 2008, 16 decisions were adopted including 7 unconditional approvals of mergers. The CCA has continued to provide the Government with assessments of draft laws as well as other expert opinions.

The Misdemeanour Court in Zagreb has completed proceedings against one undertaking entering into a prohibited agreement with another. For the first time a significant fine was imposed both against the company and the responsible persons. However, an efficient system for imposing fines to allow CCA decisions to have a deterrent effect but also leniency and judicial control have not been remedied.

Progress has been made in the area of **state aid**.

Croatia completed in June its state aid inventory and provided data for all state aid measures for the remaining sectors of aluminium, metal, textiles, leather and shoes, automobiles and tourism.

An action plan with a clear timetable for alignment of the aid schemes identified in the state aid inventory as incompatible with the obligations resulting from the SAA was submitted to the Commission in June.

With regard to the state aid enforcement record, between 1 January and September 2008, the CCA took 26 decisions and initiated ex officio monitoring proceedings to control that state aid has been granted in compliance with the applicable rules and schemes.

In April 2008 the CCA expressed its positive opinion on the scheme of a regional state aid map in accordance with its compliance with the *acquis*. The map was adopted by the Government in May 2008. This adoption facilitates the phasing out of incompatible aid schemes and their replacement with compatible support measures. This is in particular the case with the Investment Promotion Act and its implementing provisions that entered into force in 2007, and a series of incompatible fiscal aid measures for which full alignment with the *acquis* was achieved in June 2008.

In the shipbuilding sector, the CCA carried out in February 2008 an analysis of six proposed restructuring plans for the time period from 2007 to 2012. The CCA concluded that it was not possible, on the basis of these plans, to establish any prospects for long-term viability under market conditions. This assessment was submitted to the Ministry of Economy, Labour and Entrepreneurship (MELE) which revised the restructuring plans and submitted new ones to the CCA and to the Commission in May 2008. In the same month, the government adopted a Decision to privatise all Croatian shipyards. Steps taken thus far by Croatia do not provide a sufficient basis for ensuring compliance with EU and SAA rules.

In the case of the steel industry, good progress has been achieved in the privatisation process of the two steel mills. On the basis of individual business plans submitted by the mills and assessed by the CCA, the National Restructuring Plan for the steel industry was revised and adopted by the government on 30 June 2008. Provided that some minor adjustments are made, the National Restructuring Plan for steel of 30 June 2008 is acceptable in terms of Protocol 2 to the Stabilisation and Association Agreement.

### *Conclusion*

Some progress has been achieved on this chapter, in particular as regards state aid to the steel sector as well as the drawing up of a regional aid map and the alignment of fiscal aid schemes. However, significant efforts are required in particular as regards restructuring aid to the shipyards, which must be addressed in the context of their foreseen privatisation.

## **4.9. Chapter 9: Financial services**

There has been substantial progress in the field of **banks and financial conglomerates**. The Credit Institutions Act and the Act on Electronic money were adopted in September 2008 and related regulations are expected to be completed by the end of 2008. The Acts and expected subordinate legislation aim to fully align Croatian banking legislation with the *acquis*, in particular with the Capital Requirements Directive. The Acts will enter into force as of January 2009; however credit institutions should adjust their operations to the requirements of the new law by 1 July 2009, while some provisions will become applicable only upon accession. The framework for risk-focused supervision is still evolving, but the current supervisory techniques and risk management processes do not appear to pose any risks for successful Basel II implementation. Home-host supervisory coordination has been improved, although more emphasis needs to be put on cross-sector cooperation and cross-border coordination for crisis preparedness and management. The process of transforming savings and loan co-operatives into credit unions or savings banks continued at a good pace.

The Croatian Financial Services Supervisory Agency (HANFA) and the Croatian National Bank (HNB) are in the process of adoption of appropriate ordinances for layout and the content of annual accounts for entities under their supervision.

There has been some progress on **financial market infrastructure**. The Law on Settlement Finality in Payment Systems and in Systems for Settlement of Financial Instruments was adopted in September 2008 with the aim to align with the *acquis*. . Insolvency and finality rules were aligned with the *acquis*. The Act will enter into force in January, although provisions relating to allowing the provision of services by EU credit institutions by means of the EU passport will be applicable upon accession.

Some progress can be seen in the field of **insurance**, where Croatia's legislation already complies to a large extent with the EU *acquis*. New Insurance Act was adopted in July 2008 with the aim of aligning in particular with the reinsurance *acquis*. In October 2007 the Law on Pension Insurance Companies and Payment of Pension Annuities on the Basis of Individual Capitalised Savings was amended. It introduces provisions allowing a Member State entity, as sponsor, to procure their pension insurance for employees in Croatia and voluntary pension funds of MS to operate in Croatia, as of the date of Croatia's accession to the EU. It also enables pension payments to be made from Croatia into EU Member States without limitation and regulates in more detail the protection of the right to a pension after membership of a pension fund is terminated. The Law also allows an intermediary to be insured by an insurer from an EU Member State and the European Economic Area, as from the date of Croatia's accession to the EU. HANFA continues to adopt necessary secondary legislation to complete new legal framework.

Some progress can be reported in the area of **securities markets and investment services**. The new Capital Markets Act was adopted in July 2008 and will enter into force on 1 January 2009, except for some provisions that come effective as of Croatia's accession into the EU. The law aims at full alignment with the *acquis* and foresees the establishment of the Fund for the protection of investors, which would include all investment companies. HANFA has also adopted a number of implementing measures.

As regards *administrative capacity*, the National Bank's Prudential Regulation and Bank Supervision Department continued to increase staff numbers (reaching 105 in total). HANFA has strengthened its supervision department, by adding 10 new staff over the last year; it now has 122 employees, most of whom deal with supervisory tasks. Monitoring of trade on the Zagreb Stock Exchange was improved with the implementation of a new trading platform. HANFA has taken robust enforcement action in several cases, including the suspension of dubious trading in shares of a high profile company. Transparency of the insurance market was increased: all insurance companies were obliged to make their data available online for a period covering the previous three years. The Register of Leasing Objects, incorporating data on approximately 140,000 leasing objects (vehicles, vessels, aircrafts, machines and other equipment) became operational in October 2007 and is available on HANFA's web site. Nevertheless, some weaknesses remain. Disclosure of financial statements by listed companies remains inadequate. The rules to prevent market abuse are not always clear, and enforcement of these rules needs to be further strengthened. Pursuant to changes in the Misdemeanour Act and in both insurance and securities legislation, HANFA can not only propose but also directly impose pecuniary sanctions. More generally, HANFA's administrative capacity and its arrangements for consultation with the private sector need further strengthening.

### *Conclusion*

Good progress can be reported on this chapter. Legislative alignment is well underway, but additional attention is needed regarding its proper implementation. Both of the supervisory

authorities, i.e. the CNB and the HANFA, need to intensify their efforts to improve their supervision function and consultative interaction with the sector.

#### 4.10. Chapter 10: Information society and media

There has been significant progress in the field of **electronic communications and information technologies**. An Electronic Communications Act was adopted in June 2008. It is a significant step forward towards completing alignment with the *acquis* in this field, which is a key element for the accession negotiations in this chapter. Liberalisation of the sector has progressed significantly, in particular in the broadband market (growth of 53.7 % in 2007 compared to 2006 with a notable increase in unbundled loops), as well as in the fixed market with some emerging competition. Ported numbers in the fixed and in the mobile markets have also increased significantly. As a result of this, a general decrease of prices for private and business users has been observed. However, although the mobile market continues to represent the driving force behind the development of telecommunication services in the country with a penetration rate of about 120% at the end of the second quarter of 2008, the issue of construction permits and site sharing continues to create difficulties. This could endanger the future expansion of the mobile market.

The Croatian Telecommunications Agency has enhanced its capacity and organisation, among others through the creation of a new Section for Consumer Protection and Network Security in November 2007. Since July 2008, after a merger with the Postal Services Council, it operates as the Croatian Post and Electronic Communications Agency. However, there is not sufficient transparency in enforcing regulations for securing competitive safeguards to alternative operators, including cost accounting and accounting separation obligations imposed on dominant operators. Preparations in this area are well advanced.

Substantial progress has been made in the area of **information society services** and electronic commerce. An Act on Amendments to the Electronic Commerce Act was adopted in May 2008 and an Act on Amendments to the Electronic Signature Act in July 2008. The new Law on Electronic Media ensures protection of conditional access services in line with the *acquis*. A Strategy for the Development of Electronic Businesses for the period 2007–2010 was adopted by the Government in December 2007 and a Strategy from switching from analogue to digital broadcasting of TV programmes in July 2008. Preparations in this area are reaching completion.

Good progress can be reported also in the field of **audiovisual policy**. The remaining amendments to the Law on Electronic Media were adopted in March 2008 bringing it in line with the Television without Frontiers Directive and allowing the participation of Croatia in the Media 2007 programme. The Law introduced also some improvements in the regulatory framework including some safeguards against political interference and the promotion of self-regulation in the media. Public debate on media legislation, held during spring 2008, ended with a conclusion that the present legislative framework provides for a professional and independent functioning of the HRT Programme Council and the Electronic Media Council. Nevertheless, some interference in the media landscape by mainly economic and partly political interest groups has continued. As regards administrative capacity, a Media Desk was established within the Audiovisual Centre at the Ministry of Culture as a support structure for the implementation of Media Programme 2007 (2007–2013). Preparations in this area are well on track.

## *Conclusion*

Substantial progress has been made in this chapter, especially as regards legal alignment. Important steps have been taken towards liberalisation of the electronic communications market and towards media reform. However, although a good level of alignment with the *acquis* in this chapter has been reached, the substantial progress already made in regulation needs to be sustained for due functioning of the electronic communications market.

### **4.11. Chapter 11: Agriculture**

Limited progress was achieved as regard **horizontal issues**. The implementation of the Integrated Administrative and Control System (IACS) is still at an early stage. A comprehensive strengthening of administrative capacity, including staff recruitment and training as well as establishment of appropriate administrative procedures, is needed in order to ensure that direct payments for farmers can be handled correctly from the day of accession. A National Programme for the development of the Land Parcel Identification System (LPIS) was adopted in November 2007. Currently, preparatory activities for the implementation of LPIS in the whole territory of Croatia are in progress, but efforts need to be enhanced. Preparations for the Paying Agency are at an early stage. A project is on-going as regards the Farm Accountancy Data Network (FADN), but the preparation for further alignment with EU methodology needs to be accelerated.

As regards **common market organisation**, some progress can be reported on the preparation of certain sectors. The present system for supporting and regulating agriculture in Croatia differs substantially from the reformed Common Agricultural Policy as coupled direct payments still constitute the largest part of national aid. Enhanced preparations are required as regards the administration of quotas, price reporting, monitoring and in particular the EU's system of de-coupled direct payments. Some progress has been made in preparing the vineyard register.

A **national strategy for rural development** has been adopted in May 2008, which foresees the implementation of a national investment support scheme complementary to EU funds provided under SAPARD and IPARD. Croatia has continued to make progress to absorb EU funds under the SAPARD programme. However, it still faces difficulties regarding validation of implementing procedures. A rural development programme under the Instrument for pre-accession, IPARD, has been approved by Commission Decision in February 2008. Based on experience from SAPARD, progress has been made concerning the setting-up of a monitoring system, the legislative framework for operating the managing authority as well as the appointment of the managing personnel. However, substantial effort will still be necessary in order to achieve the accreditation of the IPARD Agency and conferral of management powers by the Commission which is expected in the first half of 2009. The implementation of SAPARD and IPARD creates a good basis for the setting up of the administrative structures for rural development that will be required after accession. It is however crucial that these preparations are enhanced.

Croatia is well prepared for accession in the areas of **quality policy** and **organic farming**. A new Act has been adopted for the transposition of Council Regulation (EC) 510/2006 on the protection of geographical indications and designations of origin for agricultural products and foodstuffs.

## Conclusion

Progress in this chapter has been very uneven. In the areas of quality policy and organic farming the situation is already well advanced. In rural development, good experience has been gained in the context of pre-accession assistance. However, the capacity of absorption of EU funds under pre-accession Rural Development programmes needs to be improved. Efforts need to be substantially intensified in relation to horizontal issues especially with regards to the Paying Agency and IACS including the LPIS. The present system in Croatia for support linked to production differs from the reformed CAP. This issue should be addressed urgently and alignment of the support system commenced in order to prepare a smooth transition to the CAP.

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

The Strategy for Transposition, Implementation and Enforcement of the *acquis* for Food Safety, Veterinary and Phytosanitary Policy, adopted in March 2008, provides a framework with detailed time schedules and action plans and is a key element for the accession negotiations in this chapter. It will be an instrument for the comprehensive work that is still required to ensure full compliance in this field before the day of accession.

As regards **general food safety**, Croatia has made good progress in adopting implementing ordinances based on the Food Act that is already in compliance with EU requirements. Substantial efforts are however still required to prepare secondary food safety legislation. Further efforts are required to ensure the necessary administrative and control capacity.

Good progress has continued in the **veterinary** field based on the Veterinary Act that is already in accordance with EU requirements. With regard to animal identification and registration of animal movements, which are key elements for the accession negotiations, measures have been adopted with a view to ensure a compliant system for identification and registration of bovines. Implementing activities have started for pigs, ovine and caprine animals.

Good progress has been made in the control of Classical Swine Fever by the adoption of an action plan for control and eradication based on a non-vaccination approach. The action plan which is a key element for the accession negotiations contains all necessary elements including reinforcement of the administrative capacity of the diagnostic laboratories and intensified controls. Substantial well-targeted efforts will be required to ensure the correct implementation of the action plan.

Good progress can be reported with regard to the **placing on the market of food and feed**. Croatia carried out a first assessment of all food establishments with regard to their compliance or non-compliance with EU standards. This was a key element for the accession negotiations and will enable the setting up of a national programme for the upgrading of establishments for food of animal origin, such as slaughterhouses, meat processing plants, dairies, and fish. The large majority of these establishments (including those for animal by-products) do at present not fulfil EU structural requirements and comprehensive efforts are required to bring them into compliance with EU structural requirements at accession. Efforts are also required as regards the quality of raw milk.

In the field of **animal welfare**, only limited progress has been made.

Good progress continued in the area of **phytosanitary** issues with the adoption of secondary legislation and the start of implementing activities notably for a plant passport system and authorisation of plant protection products. Progress has continued in the sector of plant protection products. Registration of products as required by the *acquis* commenced in late 2007. A strategy was adopted for the Institute for Plant Protection in Agriculture and Forestry. Work has continued to enhance the capacity of phytosanitary inspectors and the necessary IT-systems. In the seed sector programmes relating to the testing for Distinctness Uniformity and Stability (DUS) of varieties registered in the Croatian list of agricultural varieties have been set up. Substantial efforts are still required in the phytosanitary field, in particular as regards adoption of implementing legislation and the strengthening of administrative capacity.

#### *Conclusion*

Good progress has been made overall in particular with the passing of implementing legislation. Further efforts are required in particular as regards animal welfare, as well as strengthening of the administrative and inspection capacity.

### **4.13. Chapter 13: Fisheries**

Some progress can be reported in the areas of **resource and fleet management** and **inspection and control**. Implementing legislation concerning landing declarations and sales notes entered into force in January and June, respectively. The Fisheries Directorate was restructured in March to cover the main areas of the Common Fisheries Policy better and a three-year employment plan was adopted. The newly established coast guard service has taken on certain responsibilities for fisheries inspection. Some differences from the *acquis* remain in Croatia's technical measures for resource management. Gaps in fleet management include the absence of an entry-exit scheme. Installation of the satellite based vessel monitoring system (VMS) on board of the vessels concerned and establishment of the fisheries monitoring centre (FMC) need to be completed. The administrative capacity and equipment of the fisheries inspection services require substantial strengthening. Overall, preparations in the area of resource and fleet management and inspection and control have started.

Limited progress can be reported on **market policy**. Wholesale fish markets have been developed in Rijeka and Poreč. Croatia does not yet have producers' organisations and currently uses different marketing standards. Preparations in this area have only just started.

There has been no particular progress on **structural action** and **state aid**. Croatia still needs to set up and strengthen the institutional framework to implement the EU's structural policy and to prepare the required strategy documents. It will also have to end state aid which is incompatible with the *acquis*, such as the current fleet modernisation programme.

No particular developments can be reported in the area of **international agreements**. Croatia is generally implementing the recommendations issued by the relevant international fisheries organisations, such as the GFCM and ICCAT.

#### *Conclusion*

Croatia has made some progress in the field of fisheries. Overall, preparations have started. Gaps remain in the areas of fleet management, inspection and control, structural action and state aid. Croatia will need to step up its efforts to close these gaps.



#### 4.14. Chapter 14: Transport policy

Some progress can be reported in the field of **road transport**. The Law on Road Traffic Safety and the Law on Maximum Working Time, Compulsory Breaks for Mobile Workers and Road Transport Recording Equipment was adopted in May 2008.

The Government adopted the decree to increase the staff of the Ministry of the Sea, Transport and Infrastructure by 350 new employees, but the administrative capacity to enforce the rules relating to road transport *acquis*, including roadside checks is inadequate.

There has been some progress in the area of **rail transport**. Croatia signed the "Addendum to the Memorandum of Understanding on the Development of the South East Europe Core Regional Transport Network for a South East European Railway Transport Area" in December 2007. The railway network statement has been published in December 2007. Subordinate regulations remain to be drafted in order to achieve alignment with the *acquis* on safety and interoperability. Following the adoption of the Railway transport safety act in 2007 the Ministry has formed working groups for drafting the necessary implementation rulebooks. The Croatian Parliament adopted in March 2008 the National programme for railway infrastructure, covering the period of 2008-2012. Certain aspects of the railway reform as regards the railway institutions and full independence of the essential functions remain to be completed.

There has been some progress in the area of **inland waterways transport**. The Act on navigation and inland waters harbours was adopted in October 2007. In May 2008 Croatian parliament adopted the Inland waterways transport strategy for the period 2008-2018. The act addresses the recognition of EU vessel and boatmasters' certificates, as well as access to the market. The first stage for deploying river information services has been completed and further preparations in this area are underway. While relevant Ministerial regulations still remain to be enacted, the basic legislative framework has been aligned.

No progress can be reported in the field of **combined transport**.

Some progress can be reported in the area of **air transport**. The Act amending the Act on obligatory and property legal relations in air traffic was adopted in May 2008. Croatia has also ratified in May 2008 the European Common Aviation Agreement (ECAA), whose first transitional phase remains to be implemented. This will require some efforts and structural changes in the Ministry/Civil Aviation Authority. Furthermore the Civil Aviation Agency capable of effectively enforcing the *acquis* has not yet been operationally established, a supervisory authority for air traffic control has not yet been designated, the Single European Sky legislation has still to be enforced, as well as the ban on Chapter 2 aircraft, legislation on ground handling and slot allocation has not yet been aligned with the relevant Community rules.

Good progress can be reported in the area of **maritime transport**, in particular regarding safety issues. However, the detention rate of Croatian flagged vessels following port State controls in the area covered by the Paris Memorandum of Understanding remains high. Croatia has adopted in July 2008 the amendments to the maritime code as regards registration of ships and yachts. The maritime transport market remains largely closed. Legislation on maritime cabotage remains unaligned with the *acquis*.

As regards the **state aid** in this sector Croatia has not yet aligned its legislation with the relevant case law of the Court of Justice.

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

### *Conclusion*

Overall, there has been progress on alignment with the *acquis*. Croatia needs to establish a competent and effective railway regulatory body. It has to separate the essential functions from the entity providing transport services. A safety authority as well as investigation and notified bodies need to be set up as early as possible. Further alignment with EU *acquis* on road transport and on the establishment of common rules for certain types of combined transport of goods is needed. An action plan for the rapid implementation of the EU aviation legislation including reinforcing administrative capacity is required as well as alignment of the remaining legislation with that of the *acquis*.

## **4.15. Chapter 15: Energy**

There has been little progress in the area of **security of supply**. The mandatory 90-day average of stocks has not been reached. The Compulsory Stocks Agency is in operation. There are no developments in relation to the establishment of a crisis management body or emergency plans. There have been limited developments in relation to legislation on authorisation for prospection, exploration and production of hydrocarbons.

There has been progress in the area of the **internal electricity market**. Since July 2008 the electricity market has been opened for all customers. However, in practice HEP remains the only supplier of electricity on the market. There have been no developments in relation to HEP's privatisation. With Croatia's entry into the inter-TSO compensation mechanism, all transit fees have been abolished. Preparations in this area are advancing.

As regards the **state aid** Croatia has not yet aligned its legislation with the relevant *acquis* in this area.

Only limited progress can be reported in the area of **renewable energy sources (RES)**. The 2008 target of biofuels for 2008 has been set at 1.21% of the overall fuel consumption on the domestic market.

Administrative capacity in energy efficiency and RES needs significant strengthening.

There has been progress regarding gas markets. Implementing legislation related to liquefied petroleum gas (LPG) has been adopted. INA remains the only supplier of natural gas in the country.

Limited progress has been made in the field of **energy efficiency**. Implementing legislation related to energy labelling of household appliances has been enacted. Croatia still needs to ensure compliance related to high-efficiency cogeneration (CHP), energy end-use efficiency and energy services. No progress has been made in transposition of the *acquis* related to the energy performance of buildings.

Progress has been made in the field of **nuclear energy**. A fund for covering Croatia's liabilities in connection with the decommissioning of the Krško Nuclear Power Plant, including the disposal of radioactive waste and spent nuclear fuel, has been established. Implementing legislation related to the disposal and management of radioactive waste, protection of citizens and the environment, monitoring of imports and exports of materials

which may contain radioactive sources has been enacted. However, the disposal of all types of radioactive waste is still a pending issue.

Progress has also been achieved in the area of **nuclear safety and radiation protection**. In the area of radiation protection, the National Plan and programme of protection from ionising radiation has been adopted. Implementing legislation related to the monitoring of radioactive substances in the environment, food, residential and working environments has been adopted. In addition, implementing legislation in the measurement and protection of workers and citizens exposed to ionising radiation, quality assurance and other issues related to radiological and physical safety of sources of ionising radiation has been ratified. Progress in this area is advancing well.

A new organisational structure for the State Office for Nuclear Safety, and actions to further align the legislation on radiation protection with the *acquis*, are underway. However, further efforts are required to strengthen administrative capacity of the nuclear regulatory bodies and to ensure adequate division and coordination of responsibilities between the Ministry of Health and Social Welfare and the two State Offices for Nuclear Safety (SONS) and Radiation Protection (SORP).

Overall, alignment with the *acquis* is well advanced.

### *Conclusion*

Overall, there has been good progress. However, significant efforts are still needed to align with the *acquis*, particularly in energy efficiency. Sustained efforts will also be needed for meeting Accession Partnership priorities related to the strengthening and the independence of the regulatory authority and administrative capacity, in particular in energy efficiency and renewable energy sources.

## **4.16. Chapter 16: Taxation**

No progress can be reported in the area of **indirect taxation**. Croatia's legislation on VAT remains partially in line with the *acquis*. Substantial changes are needed, in particular as regards reduced or zero rates, the scope of the reduced rates and of exemptions, the exclusion of free zones from the fiscal territory, the special schemes and the lack of legislation on VAT refunds to non-established traders. On excise duties substantial changes are needed on product coverage, rates and duty suspensions. In October, Croatia agreed with the Commission a solution for eliminating the discriminatory elements of its excise duty system for cigarettes, so to address its incompatibility with the SAA. In the area of indirect taxation Croatia has not addressed the Accession Partnership priorities.

No progress has been made in the area of **direct taxation**, where Croatia has not addressed the Accession Partnership priorities.

No progress can be reported on **administrative cooperation and mutual assistance**.

There was some progress with **operational capacity and computerisation**. The excise department in the customs administration was re-organised into four units, to mirror the structure of the EU legislation. Attention should be paid to adequate staffing of this department, with a view to establishing the system for movement under suspension. Work on IT interconnectivity has progressed, albeit with some delays, and projects to develop the VAT information exchange system and the excise movement control system have started. Both the

tax and customs administrations remain heavily dependent on external expertise on IT matters and in need of reinforcement of their internal capacity.

### *Conclusion*

There has been very limited progress on this chapter. No progress was made on legislative alignment. Even though the overall structure of the tax legislation is similar to the *acquis*, substantial efforts are required in all areas. Croatia has agreed with the Commission a solution for eliminating the discriminatory taxation of cigarettes. Substantial further efforts are also required to strengthen the administrative capacity, including regarding IT interconnectivity.

#### **4.17. Chapter 17: Economic and monetary policy**

Significant progress can be reported on alignment with the *acquis* governing **monetary policy**. Croatia adopted a revised Law on the Croatian National Bank (CNB) aimed at full alignment to the relevant *acquis*. The new Law provides for the full independence of the central bank, in particular by clarifying the issue of accountability of the central bank. The new law also regulates its future integration into the European System of Central Banks. Furthermore, the new legal framework strengthens the institutional, financial and personal independence of the CNB.

Good progress was made regarding the elimination of the legislative provision providing for *privileged access for public authorities to financial institutions*. In March 2008, amendments to the Act on the Croatian War Veterans and their Family Members Fund were adopted. As of the date of Croatia's accession into the EU, the Fund may invest its assets not only into debtor securities of the Republic of Croatia and securities the Republic of Croatia is guaranteeing but also into securities issued by the EU or OECD member states without restrictions. However, some provisions that give rise to privileged access for public authorities to financial institutions still remain in Croatian legislation, notably in the Deposit Insurance Act.

In March 2008 the Croatian National Bank (CNB) issued a Decision providing the legal basis for establishing a National Centre for Fight Against Counterfeiting, a National Centre for Analysis of Bank Notes and a National Centre for Analysis of Coins, within the CNB. The purpose of these centres will be to undertake and implement measures for the prevention of counterfeiting and detection of counterfeited coins and bank notes. Currently these tasks are performed by a unit in the Ministry of Interior. Overall, preparations in the field of monetary policy remain well on track.

In the area of **economic policy**, the country has made some progress in its alignment with the *acquis*, particular in improving the institutional and technical capacity for setting up medium-term macroeconomic and fiscal frameworks. Croatia submitted its fourth Pre-Accession Economic Programme, covering the period 2008-2010, in December 2007. It presents a largely sound and coherent medium-term macroeconomic and fiscal framework and a broad agenda for structural reforms. Croatia submitted its fourth fiscal notification in March 2008. Reporting of fiscal data on the basis of ESA 95 has improved. However, with respect to policy implementation, an ad-hoc approach to economic policies has often prevailed and a deepening of structural reforms has not figured among the governments' top priorities. The structural reform agenda has moved slowly and there has often been a gap between legislative intent and actual implementation. Policy coordination within the government as well as the government's communication with the Croatian National Bank (CNB) has not been systematically enforced. Overall, in the field of economic policy Croatia has made further

progress in designing medium-term economic policy strategies, but the actual implementation of core reforms has often been weak..

### *Conclusion*

There has been significant progress in the area of economic and monetary policy. Overall alignment with the *acquis* in the area of economic and monetary policy is well advanced.

## **4.18. Chapter 18: Statistics**

Good progress can be reported concerning the **statistical infrastructure**. The Central Bureau of Statistics (CBS) has been placed under the direct responsibility of the Prime Minister. This will strengthen its coordinating role. Also the budget of the CBS for 2008 has been substantially increased. The Annual Implementation Plan for Statistical Activities in 2008 and a programme of statistical activities covering 2008–2012 (mid-term plan) were adopted in May 2008. Cooperation between the CBS and the other main producers of official statistics has improved. As regards administrative capacity, a new Director General of the CBS was finally appointed in May 2008. Individual training plans for CBS staff are being developed. However, there has been only little progress in the actual increase of staff. Most of the new posts have not been yet filled. Notably the IT department has suffered a high rate of departures of skilled staff and has a lot of problems in recruiting new staff. Moreover, the reorganisation of the regional statistical offices has not yet taken place, and the preparation of a dissemination strategy of statistics is advancing only moderately. The Accession Partnership priority has been partially met. Preparations in this area are on track.

Little progress can be reported in the field of **classifications** and registers. The classification according to NACE Rev.2 has not been implemented due to IT staff shortages. The quality of the business register is being improved but remains far from satisfactory. Preparations in this field are only moderately advanced.

Good progress has been made in the area of **sectoral statistics**. As regards social statistics, a national methodology for a survey on income and living conditions is being developed. Good progress has been achieved in labour force statistics, government finance statistics, external trade statistics and in the timely transmission of data to Eurostat. Concerning agricultural statistics, some progress has been made, in particular with a view to obtaining comparable agricultural structure, agromonetary and dairy data. Nevertheless, the methodology and organisational set-up for collecting agricultural statistics are not yet in line with the *acquis*. In the area of macro-economic statistics, key national accounts indicators and the methodology used are still not in line with the *acquis* (ESA 95). These are, together with agricultural statistics, key elements for the accession negotiations on this chapter. The structural business statistics are being revised with the objective of providing data on all sectors, including at regional level. However, a full alignment of the business statistics with the *acquis* has not yet been completed. The Accession Partnership priority has been partially met. Preparations in this area are well on track.

### *Conclusion*

Overall, good progress has been made on modernising the statistical infrastructure. A satisfactory level of legal alignment has been reached. However, gaps remain in terms of strengthening the administrative capacity for producing statistics. As regards sectoral statistics, the key areas of agricultural and macro-economic and business statistics are not yet

in line with the *acquis*. Continued efforts are required to align legislation with the *acquis* and to implement and enforce it effectively.

#### 4.19. Chapter 19: Social policy and employment

There has been limited progress in the area of **labour law**. Amendments to the Act on Employment Mediation and Unemployment Rights were adopted in July 2008 aiming at addressing shortcomings in the field of part-time work. Legislation aiming at transposing the *acquis* in the areas of European Works Council, the European Company, the European Cooperative Society and the protection of employees in the event of the insolvency of their employer has been adopted. As regards administrative capacity, a new Regulation on the internal organisation of the Ministry of Economy, Labour and Entrepreneurship (MoELE) was adopted in March 2008 in view of strengthening the organisation of the Directorate for Labour and the Labour Market and hiring additional staff, but its implementation is lagging behind. In general, shortcomings persist as regards legal alignment and administrative capacity. The amendment of the Labour Act is still outstanding. This is a key element for the accession negotiations on this chapter. The State Inspectorate is lacking appropriate resources. Preparations in this area are on track.

Good progress can be reported in the field of **health and safety at work**. The Act on Amendments to the Occupational Safety and Health Act was adopted in July 2008. This is a key element for the accession negotiations on this chapter. Legal alignment has continued also with the adoption of legislation aiming at transposing the *acquis* on use of work equipment, on minimum requirements for work on board fishing vessels, on noise, on electromagnetic fields and on temporary or mobile construction sites. However, implementation and enforcement capacity is still not sufficiently developed, and sufficient funding of implementation remains a problem. The Labour Inspectorate is not sufficiently mobile either. In order to remedy the situation, the Regulation on the internal organisation of the State Inspectorate was amended in December 2007 allowing for an additional hiring of 53 labour inspectors (27 in the area of labour relations and 26 in the area of safety at work). Preparations in this area are well underway.

As regards **social dialogue**, there has been some progress. Tripartite social dialogue is already well established, and the influence of social dialogue on the decision making process and policy design has slightly improved. Tripartite social dialogue has resulted, *inter alia*, in the Act on minimum wage. Awareness-raising and training activities have continued, especially as regards mediation of labour disputes. However, the existing autonomous collective bargaining still takes place mainly at company level. Sectoral social dialogue continues to be poor, and agreements at this level are rare. Representativeness criteria for participation of trade unions in collective bargaining have not been adopted yet. The capacity of social partners continues to be weak. Preparations in this area are moderately advanced.

Good progress has been made in the area of **employment policy**. The Joint Assessment of Employment Policy Priorities (JAP) was signed in May 2008. It examines the main strengths and challenges for the Croatian labour market with a view to EU accession and Croatia's future participation in the EU employment strategy. In the framework of the National Employment Action Plan for 2005–2008, funds earmarked for the implementation of active labour market measures under the 2007 Annual Programme for Employment Incentives have been increased. The fight against undeclared work has continued allowing a continuing rise in the employment rate (57 % in 2007 compared to 55.4 % in 2006). The unemployment rate has continued to fall (9.6 % in 2007 compared to 11.2 % in 2006). However, youth and long-term

unemployment remain persistent challenges. Also regional disparities are still considerable, and the qualification and skills levels of the Croatian labour force are lower than in the EU. Preparations in this field are well on track.

There has been some progress in the preparations for the **European Social Fund**. Activities are ongoing to refine the internal procedures and to complete the setting up of administrative capacities in the Operating Structure. Training plans are being developed. In March 2008, a Directorate for International Cooperation in the Field of Labour and Social Security was established in the MoELE to perform the tasks of the body responsible for the Operational Programme for IPA component IV (Human Resources Development) and for priorities and measures. However, administrative and management capacity is not yet sufficiently developed with a view to the future implementation of the ESF. This is a key element for the accession negotiations on this chapter. Preparations in this field are moderately advanced.

Some progress can be reported in the field of **social inclusion**. A second Joint Inclusion Memorandum (JIM) follow-up seminar was held in March 2008 in Zagreb. A National Implementation Plan for Social Inclusion (2007–2008) was adopted by the Government in April 2008 and the National Implementation Report on the JIM follow-up process 2007–2008 was adopted in July 2008. A strategy on decentralisation of social services has been developed, and some activities have been undertaken in the first phase of a long process in securing de-institutionalisation for particular target groups, namely the elderly.

However, the overall progress in meeting the priorities and measures set out in the JIM has been slow, and the use of a coherent monitoring and evaluation system to assess policy reforms in this field continues to be weak.

As regards administrative capacity, the Regulation on the internal organisation of the Ministry of Health and Social Welfare was adopted in March 2008 establishing two new departments in the Ministry related to social inclusion. However, the position of the Director of the Department for Social Welfare at the Ministry has not yet been filled. As regards people with disabilities, an Ombudsman for Persons with Disabilities was appointed by the Parliament in May 2008 and its office is being set up. A Civil Service Recruitment Plan for 2008 was adopted in March 2008 aiming at the employment of 128 persons with disabilities. However, budgetary constraints continue to limit the scope of the rights of people with disabilities to health and special care and their social integration. The cooperation of the Government with the civil society organisations is not sufficient to create an adequate net of community-based services. (*See Political criteria – Economic and social rights*) Preparations in this area are moderately advanced.

Limited progress can be reported in the field of **social protection**. Reforms in the pension and health care systems are ongoing. As regards pensions, progress is being made in extending the effective working life and in decreasing the share of retirement contributions in GDP. However, universal coverage and adequacy of pensions is not yet ensured. Poverty among the elderly as well as the large number of women of pensionable age not receiving pensions remain a concern. Preparations in this field have started.

There has been good progress in the field of **anti-discrimination**. An anti-discrimination act was adopted in July 2008 aimed at completing legal alignment in this field. This is a key element for the accession negotiations on this chapter. A National Programme for the Protection and Promotion of Human Rights 2008–2011 was adopted in November 2007, and the National Plan to Combat Discrimination in September 2008. However, the level of

protection against discrimination in practice and its judicial prosecution is still not in line with EU standards. Vulnerable groups and ethnic minorities, particularly the Serb and the Roma minorities, continue to face significant discrimination in economic and social life (*See Political criteria – Economic and social rights*). The Ombudsman's office has not yet been transformed into an independent Equality Body. The limited statistics currently available do not allow monitoring of discrimination on different grounds, as required by the *acquis*. Preparations in this field are on track.

Good progress can be reported on **equal opportunities**. A new Gender Equality Act was adopted in July 2008 after the Constitutional Court issued a decision in January 2008 to abrogate the former Act on the grounds of its formal non-compliance with the Constitution of Croatia. This is a key element for the accession negotiations on this chapter. Legislation was also adopted in March 2008 aiming at transposing the *acquis* on statutory social security as well as in July 2008 in the field of parental leave. Awareness-raising activities on gender equality have continued in different areas. However, the Ombudsman's office has not yet been transformed into an independent Equality Body. Also the effective implementation of gender equality policies is not always ensured (*See Political criteria – Economic and social rights*). Preparations in this field are well advanced.

### *Conclusion*

Good progress has been made on this chapter. A good level of legal alignment has been reached. Gaps remain in relation to completing legal alignment. Strengthening the administrative capacity in good time before accession to ensure proper implementation and enforcement of the *acquis* in this field remains the key element for the accession negotiations on this chapter.

## **4.20. Chapter 20: Enterprise and industrial policy**

Substantial progress has been made in the area of enterprise and industrial policy principles. Croatia adopted a comprehensive industrial strategy in line with the *acquis*.

As regards SME policy, Croatia continues to implement the actions and guidelines of the European Charter for Small Enterprises. Overall, it has made considerable progress in all areas of the Charter. The implementation capability in this field is relatively well structured and resourced and framed in a concise set of SME strategies and operational plans. There is a better distribution of roles between the Ministry of Economy, Labour and Entrepreneurship (MELE) and the SME agency (HAMAG), whilst HAMAG should increasingly be taking on a much broader role in SME policy implementation. Croatia has made progress in further aligning with the EU SME definition but full alignment still needs to be ensured.

As regards the business environment, the HITRO.HR initiative to speed up company registration, and HITRO.REZ to cut regulatory burdens on SME's are encouraging and require further strengthening. Despite these initiatives, Croatia still has to make further efforts in order to reduce costs and time of registration and licensing. The development of online registration for crafts (e-crafts) is positive and could be extended to all types of companies.

Croatia has made substantial progress on **enterprise and industrial policy instruments**. Croatia joined the CIP Community Framework programme in October 2007 and it has submitted a successful bid under the Enterprise Europe Network which the programme finances. Croatia has made progress in further aligning its legislation with the Directive on combating late payments but the alignment still needs to be completed. Croatia is advancing



with the introduction of online-applications and e-services, for various payments and applications, a smart card for business services and a web-based “business navigator”. There is recognition of the importance of a further push in the fields of competitiveness and innovation.

Croatia has made progress with regard to **sectoral policies**. It has developed sectoral approaches and strategies in key sectors, such as the textile industry, leather and leather products, the chemical industry, and wood processing industry. Croatia has successfully privatised its steel sector; the national restructuring plan for the steel sector and individual business plans require full implementation. Croatia has taken the decision to privatise its shipbuilding industry, but further significant efforts will be needed to fully restructure it (*see competition policy chapter*).

#### *Conclusion*

Croatia has made good progress on this chapter. There has been good progress on SME policy as well as with the industrial strategy and restructuring of the steel industry. In other sectors, such as shipbuilding, significant efforts are required.

#### **4.21. Chapter 21: Trans-European networks**

Croatia has made good progress in the development of the **transport networks**. In July 2008 Croatia and the European Commission came to an agreement on the future Croatian TEN-T network and priority projects of European Interest in the framework of this network. This will be the focus of the future Croatian investments in upgrading the relevant infrastructure to the TEN-T standards.

The Trans-European Network in Croatia will consist in a multimodal network including main road, rail, inland waterway, river ports, seaport and airports of the country.

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

There has been progress on telecommunications networks. The Croatian Parliament ratified in March 2008 the Memorandum of Understanding between the Republic of Croatia and the European Community on the participation of the Republic of Croatia in the Community Programme “ICT Policy Support Programme (ICT PSP) of the Competitiveness and Innovation Framework Programme (2007 to 2013)” and it entered into force in May 2008.

#### *Conclusion*

Overall, Croatia has made good progress regarding the development of the transport and energy networks in line with the design and objectives of the TEN – Transport network and TEN – Energy network.

#### **4.22. Chapter 22: Regional policy and coordination of structural instruments**

Some progress can be reported on the **legislative framework**. In March 2008, the Croatian Government adopted an Action Plan for meeting EU cohesion policy requirements as key element in the accession negotiation under this chapter. The action plan describes the state of play of preparations, sets out all the measures that Croatia needs to take before its accession and demonstrates its recognition of the main challenges and key issues to be addressed.

Progress can also be noted as regards alignment of national legislation with Community rules in the areas of public procurement, – with the new Public Procurement Act in force since January 2008 – competition, state aid and the environment. (*See also the relevant Chapters.*) However, Croatia still needs to pursue its efforts in order to meet the regulatory requirements for cohesion policy, mainly by amending the Budget Act to ensure full multi-annual budget programming and budget flexibility and by adopting the Regional Development Act that will provide a broad legal framework for implementation of the regional policy. Preparations in this area are fairly advanced.

There has been good progress with the **institutional framework**. An application to the Commission for the accreditation of the institutional set up for the implementation of the structural funds precursor instrument IPA (Instrument for Pre-Accession Assistance) components III and IV after formal designation of the structures was submitted in April. An Audit Authority, as a separate and independent agency, was appointed in June. Croatia has also identified the coordinating authority, certifying authority, audit authority and the managing authorities and intermediate bodies that will be responsible for managing operational programmes under the future Structural and Cohesion Funds. Croatia needs to formalise (by legal act) this designation of institutional structures; it needs to ensure an adequate separation of functions in particular within ministries, as applicable between Managing Authorities and intermediate bodies. Croatia also needs to complete the full designation of structures notably as regards regional level implementation structures but also as regards the intermediate bodies.

As regards territorial organisation, Croatia has introduced a classification establishing three statistical and planning regions at Nomenclature of Territorial Units for Statistics (NUTS) II level, in line with the relevant regulations and with the Commission's suggestions.

Preparations in this area are advancing.

There has been some progress in the area of **administrative capacity**. Croatia is carrying out a systematic analysis of the organisational, staff and training needs for the IPA and Structural Funds. A training strategy for the Structural Funds preparations was prepared in June. However, capacity building needs remain large in some ministries and strengthening administrative and absorption capacity remains a priority for Croatia. The current lack of institutional capacity has directly influenced absorption capacity with respect to ISPA. In order to successfully absorb IPA and Structural Funds in the future, significant strengthening is required. Project preparation and strengthening of the organisational and managerial capacities of future beneficiaries also needs to be increased at all levels, including the local government level. Ownership should be developed and ensured at all appropriate levels, especially at local level. Preparations in this area are advancing.

Some progress can be reported in the area of **programming**. Inter-ministerial working groups under the coordination of the Central State Office for Development Strategy have drawn up a Strategic Coherence Framework 2006-2013 and 4 Operational Programmes, which were adopted by the Commission in November/December 2007. Croatia's Action Plan for meeting EU cohesion policy requirements defines practical steps to prepare the National Strategic Reference Framework along with eight sets of operational programmes. Efforts need to be made to ensure that national and sectoral strategies are coordinated within programming documents. Croatia needs to considerably improve its capacity for the timely preparation of good quality and mature project proposals submitted under Phare programmes as well as for IPA component III and IV operational programmes. Preparations in this area are advancing.

Progress was made in the **monitoring and evaluation** of the operational programmes. Operating structures have set up sectoral monitoring committees (SMC) to monitor the implementation of OPs. The first two SMC meetings for each OP were held in December 2007 and June 2008. The membership and rules of procedure of the SMCs have been agreed with the Commission. The first meeting of the (all components) joint IPA committee was held in July 2008. Croatia is still at an early stage of establishing its electronic monitoring system. Substantial work still lies ahead. It still needs to define functionalities of the system, formulate technical specifications, obtain technical assistance for setting up its system and make it operational. Preparations in this area are advancing.

Although some progress can be reported in the area of **financial management and control** (see also chapter 32 – *Financial control*), Croatia is still at an early stage of establishing its financial management and control systems for the future Structural and Cohesion Funds. Croatia needs to build up its capacity in these fields. Preparations in this area are at an early stage.

### *Conclusion*

Some progress can be reported in this chapter. Croatia still needs to make efforts to establish the institutional and administrative capacity necessary to meet the regulatory and operational requirements stemming from Community cohesion policy. Overall, Croatia is partially aligned with the *acquis* in this chapter.

## **4.23. Chapter 23: Judiciary and fundamental rights**

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

As regards the *independence of the judiciary*, there has been some progress. The State Judicial Council's (SJC) capacity to manage the selection of judges has been marginally improved. However, the capacity to systematically interview candidates remains limited. Amendments to the Courts Act and a new Act on Trainees in Judicial Bodies and the Bar Exam were passed which foresee the introduction of improvements to the procedure for the appointment of judges and judicial trainees. Currently, the selection procedure for judges and prosecutors, judicial trainees, and court advisors remains deficient, lacking transparency and the application of uniform, objective criteria. The provisions on penal immunity for judges have not been re-assessed in line with the need for transparency and accountability within the judiciary.

The evaluation of the work of judges has improved, based *inter alia* on the methodology for assessing judges' performance adopted in September 2007. The work of the judges is evaluated annually and non-fulfilment of the quota of decisions may lead to disciplinary procedures. This methodology is also used to evaluate the performance of judges under the five year probation period, which remains in place. So far, only four judges were not appointed permanently

As regards the *impartiality* of the judiciary, the State Judicial Council has continued to conduct disciplinary procedures initiated by court presidents and the Ministry of Justice. In 2007, there were nineteen disciplinary proceedings resulting in two reprimands, four fines and one acquittal. Four cases were suspended or withdrawn and eight cases are on-going. Further information on the legal grounds of the cases is not available. A new code of ethics for attorneys was adopted in February 2008. The code introduced an annual reporting obligation on disciplinary procedures conducted by the State Prosecutor Council. This should improve

the transparency of disciplinary proceedings against attorneys, which has hitherto been lacking .

As regards *professionalism and competence* in the judiciary, a full time Director of the Judicial Academy was nominated in May 2008. The Judicial Academy's budget was increased. The Judicial Academy, supported by an Advisory Board and Programming Council has developed a training policy. This introduces regular training needs assessments and adaptation of the training programmes to up-coming legislation and EU acquis. However the Judicial Academy still lacks staff. The Regional Centres of the Judicial Academy still lack resources and adequate premises.

In relation to the *efficiency of the judiciary*, the Supreme Court continues to monitor closely the backlog and supports the transfer of non-disputed enforcement cases to public notaries as well as mainly civil cases to less burdened courts. Changes to the Misdemeanour Act entered into force in January 2008 aimed at relieving misdemeanour courts of minor cases by transferring work to administrative bodies. The backlog of pending cases before all courts has been reduced by around 7% to 937,000 cases. Efforts have been made to accelerate the solving of old cases and establish more reliable statistics on the backlog.

However, statistical tools have principally been improved in relation only to municipal court cases. Previous reductions in the backlog have not been sustained and the number of old cases remains high. The roots of the backlog and lengthy proceedings have not been tackled adequately. The reform of civil procedure started in 2003 has not shown clear results. While further amendments to the civil procedure code were adopted in July, there has been no proper assessment of the previous measures' impact on case duration. Misdemeanour cases account for 37% of the backlog. More than half of these cases are dismissed because of the statute of limitation. Changes to the Misdemeanour Act extended the statute of limitation for misdemeanour cases from two to four years. While this will lead to the expiry of the statute of limitation in fewer cases, it could have a negative impact on the case backlog. The handling of administrative cases also continues to face particular challenges. The Administrative Court still needs to be made a court of full jurisdiction.

One of the main problematic areas remains enforcement cases, out of which approximately 50% fail because of the lack of a proper notification system to the parties. Reform of the system of enforcement of court decisions has begun. However, this continues to constitute a major obstacle to the efficient functioning of the courts.

There continues to be limited progress in the rationalisation of the courts network and many issues remain open. Steps taken so far are unambitious. The law on the seat and jurisdiction of courts adopted by Parliament in July 2008 foresees full rationalisation of municipal courts by 2019 with a reduction from 108 to 67 municipal courts. It remains unclear how this rationalisation will be implemented in practice. There is no plan for the rationalisation of other types of court: commercial courts, misdemeanour courts, county courts or state prosecution offices.

With regard to the infrastructure and equipment of courts, there has been limited progress. The pilot testing of the integrated case management system (ICMS) was finalised in four courts and testing has begun in several other courts. However, the foreseen roll-out of ICMS to 60 courts by 2009 is behind schedule. Misdemeanour courts continue to suffer from a shortage of equipment and a very low standard of premises.

The system of judicial inspections has shown good results. However the inspections have been carried out mainly in municipal courts and not in other courts or prosecution offices. With only five part-time inspectors, the Ministry of Justice does not have the capacity to enlarge the inspections to other courts.

The introduction of court-mediation in the Commercial court has been successful. The same concept was introduced at 8 municipal courts in 2007. However the number of mediation cases has been increasing rapidly and judges have difficulty in dealing with them. The incentive to deal with mediation cases is lacking and the backlog of cases has started to increase, especially at Zagreb Municipal court. There is no proper mediation strategy in order to focus ADR out-of court.

Implementation of the *judicial reform strategy* has continued even if adequate monitoring of its measures has not been possible due to weak administrative capacity. A revised Action Plan addressing all major reform issues was adopted in June 2008. However, in certain areas it lacks measurable objectives that will allow effective monitoring of its implementation. The Strategic Planning unit in the Ministry of Justice has become a Directorate in charge of the monitoring of the reform of justice and anti-corruption strategy and has been reinforced with additional staff. However, there is no statistical department nor a Directorate for IT issues to cover the roll-out of the case management system in the courts. There has been a lack of leadership and ownership in reform implementation.

There has been some progress in the area of **anti-corruption** policy and measures.

A revised anti-corruption strategy as well as an action plan containing specific measures in a number of fields prone to corruption was adopted in June 2008. A new coordination system based on a working group at the level of State Secretary is now in place aimed at improving coordination of all Ministries and other bodies involved in the implementation of the plan. The Strategic Unit which had been created at the Ministry of Justice in order to follow the implementation of the previous plan has been up-graded to the level of Directorate and strengthened with additional staff. The new strategy and action plan are an improvement on the previous national anti-corruption programme and its mini action plans. However, the action plan lacks measurable objectives that will allow an effective monitoring of its implementation. It is too early to evaluate the concrete impact of administrative strengthening of the Ministry of Justice.

New members of the National Council to monitor the implementation of the plan were appointed after the November 2007 elections. Its new Chairman declared the intention to break with the previous practice and to increase the pro-active approach of the Council. The structure of the Council will be strengthened with administrative staff. However, the concrete effects of the guiding role which the Council should have within the anti-corruption policy have not yet materialised.

The legal framework to combat corruption is largely in place. Amendments to the law on Conflict of Interest further strengthen the legal tools to fight corruption, including a limited increase in sanctions. However, an adequate system to deal with conflicts of interest remains to be put in place. The principle of conflict of interest is little understood at all levels of public administration. There are still no public written, interpretive guidelines for public officials. The Committee for the Prevention of Conflict of Interest continues to be beset by problems, including the resignation of its chairperson following corruption allegations. Due to the lack of administrative capacity, this committee conducted only a limited number of conflict of

interest proceedings. The discussion on conflict of interest remains a partisan issue with a consequent negative impact on its policing. There is insufficient supervision and control with regard to the implementation of asset declarations. Although a Law on Financing of Political Parties is in place, the important issue of financing of election campaigns has not been fully addressed. The Government established a working group in September to analyse the existing law.

In terms of suppression of corruption, the anti-corruption body, USKOK, has continued to become more active. The number of USKOK investigations has increased and indictments issued in some important cases. USKOK's role is more widely acknowledged and reports to it of suspected corruption have increased significantly, particularly as regards abuse of office cases. However, few actual prosecutions have followed. Law enforcement agencies and other state bodies involved in the fight against corruption continue to be more reactive than proactive. Further efforts are required in tackling high level corruption as well as in the field of public procurement. The police need to become more effective in the fight against corruption and organised crime. Inter agency cooperation requires further improvement.

Overall, corruption at the political, economic and institutional level, including the judiciary, as well as the general tolerance of petty corruption remains widespread and poses a serious problem. Corruption in Croatia is aided by a lack of good governance, transparency and accountability in public administration and by a lack of ethics codes and codes of conduct in the public and private sectors. A culture of political accountability is lacking. There has been some progress with the promotion of integrity within the public administration but this needs to be further strengthened. Awareness-raising activities coordinated between all bodies involved in the national anti corruption programme also need to be further pursued.

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

As regards the right to *protection of personal data*, the Parliament passed amendments to the Data Protection Act in March 2008 aimed at aligning it with the *acquis*, in particular the establishment of personal data protection officers. However, full alignment with the Data Protection Directive and the Council of Europe instruments remains to be completed.

Some steps were taken to address shortcomings in *prison conditions*. A shortage of prison staff and capacity remains, however.

*Freedom of expression* including freedom and pluralism of the media continue to be provided for in Croatia. However, editors and journalists continue to report undue political pressure. There have been cases of threats and attacks against journalists, particularly those working on corruption cases or organised crime.

The Office of the Ombudsman for Persons with Disabilities was created and a National Implementation Plan on Social Inclusion 2007-2008 produced. However, continued efforts are needed as regards *socially vulnerable and/or persons with disabilities*. In the area of mental health, the policy of providing care through community-based services instead of in institutions has shown no tangible progress.

A comprehensive law on *anti-discrimination* was adopted in July 2008, signifying important progress. However, the level of protection against discrimination in practice and its judicial prosecution is not yet in line with EU standards. The functioning of the police and institutions of the health and social system displayed certain weaknesses.

Plans aimed at improving *women's and children's rights* have continued to raise awareness. However, further improvements in implementation need to be made. Implementation measures regarding the protection of children's rights also have to be accelerated.

A new Law on Legal Aid as well as legislation on attorneys' tariffs were adopted aimed at improving *access to justice*, which has been hampered over the past year by limits of the existing system of legal aid, high lawyers' fees and weaknesses in the judicial system. Provision of free legal aid under the new system is foreseen as of February 2009. Implementation of the law will require new administrative structures to be set-up, including the employment of 53 new civil servants. In addition, several by-laws are to be adopted including those regarding the remuneration for attorneys.

Some progress has been made with regard to *minorities*. An action plan for implementation of the Constitutional Law on National Minorities (CLNM) was adopted as was a recruitment plan for 2008 for minorities in the State administration. Funding for minorities was further increased. The Roma minority has continued to receive attention, with improvements in pre-school education. All eight minority MPs are in the governing coalition, and a Serb has been appointed to one of the Deputy Prime Minister posts.

However, many problems remain for minorities. Croatia needs to encourage a spirit of tolerance towards the Serb minority and take appropriate measures to protect those who may still be subject to threats or acts of discrimination, hostility or violence. Minorities continue to face particular difficulties in the area of employment, both in terms of under-representation in state administration, the judiciary and the police as well as in the wider public sector. The Roma minority faces particularly difficult living conditions and challenges remain in the areas of education, social protection, health care, and employment. Legal provisions and programmes need to be implemented with more determination, and adequate monitoring assured, especially in the area of employment.

There has been some progress on *refugee return* issues. An action plan for the accelerated implementation of housing care programmes was adopted with a target completion date of end 2009. Important decisions were taken opening up the possibility of validating pension rights. Reconstruction of housing has continued. The target for 2007 to provide 1,400 accommodation units out of a total of 12,500 applications under the housing care programmes for former tenancy rights holders has been largely met. However, implementation of these programmes remains weak. The Government's implementation targets are behind schedule. Only 12% of cases have been resolved definitively in the urban areas. Efforts to create the economic and social conditions necessary for the sustainability of refugee return need to be accelerated.

As regards EU citizens' rights, amendments to the Aliens' Act were passed aimed at aligning with the *acquis*. However, further legislative changes will be needed to achieve full alignment.

#### *Conclusion:*

Croatia has made some progress on this chapter. Reforms in the judiciary continue but at only a relatively slow pace. Significant challenges remain. Most tools are in place to fight against corruption but, given the scale of the problem, these are not being deployed with sufficient vigour. Legal provisions on fundamental rights are in general adequate, but despite some progress, a number of important challenges remain in terms of implementation.

#### 4.24. Chapter 24: Justice, freedom and security

There has been some progress in the field of **migration**. The Action Plan for the implementation of the migration policy was adopted by the Government in May 2008. It covers a short period (2007-2008) and tackles issues such as legal and illegal migration, protection of asylum seekers and other refugees, and suppression of trafficking in human beings. The new Aliens Act, entered into force in January 2008. It restricts *inter alia* the conditions for a temporary residence permit and for family reunification for non-Croatian citizens.

The **illegal migration** deportation centre at Jezevo remains overcrowded. The number of illegal migrants fell in 2007 to about 4,000 compared to 5,564 in 2006. However, there has been an increase in illegal unaccompanied minors, who make up 12% of total illegal migrants in 2007. There are no specific treatment and accommodation facilities for minors and vulnerable groups. The number of forced returns has increased by 3% (2,439 cases in 2007 compared to 2,348 in 2006). There has been no increase in the number of staff at the Ministry of Interior for dealing with forced return and illegal migrants.

Croatia has 24 readmission agreements in force. Seven of these still have to be aligned with the EU model. Further readmission agreements are to be finalised with Serbia, Montenegro, Slovakia, Ukraine, Moldova and Cyprus.

Some progress can be reported in the field of **asylum**, as the new Asylum Act entered into force in January 2008. The Commission for asylum (second instance appeal body replacing the former Government Commission for asylum) was formed in April 2008. A full-time president of the Commission was appointed, together with four part-time members, two of whom come from civil society and the academic world. Although this is a step in the right direction, there is still concern regarding the independence of this Commission, given the oversight role of the authorities in the appointment process. In March 2008, five implementing acts for the Ministry of the Interior were adopted covering accommodation forms and data collection; legal aid, financial aid, and medical examinations. However, further alignment of the legislation with the *acquis* in this area is needed.

The case workers in the Ministry of the Interior have received training on the Refugees Convention and the EU *acquis*, as well as a manual on case handling, the direct outcome of which is the improved quality of the procedure for determining refugees' status. On the other hand, the restricting of personal interviews in the accelerated procedure for asylum seekers is a matter of concern.

The number of asylum seekers in Croatia continues to increase, with 170 procedures in 2007 (compared to 105 in 2006) and already 50 for the first quarter of 2008. Croatia granted asylum status in two cases. Even if Croatia is still a transit country (50% of the asylum seekers leave Croatia before their case is settled), the increase in applications is likely to expand after Croatia's accession to the EU. Current staffing levels are not adequate to meet this future demand.

To date, a number of asylum seekers applying at the border or at the illegal migrants' detention centre of Jezevo have been detained and convicted of illegal entry. This shows a very restrictive interpretation of the new law.

Some progress has been made concerning **Visa policy**. Following the new Aliens Act, a new Regulation on the Visa Regime entered into force in May 2008, which further aligned with



EU rules. The visa requirement for citizens from Serbia and Montenegro has again been suspended, until end of 2008. IKOS, the information system which forms the basis of the future Croatian Visa Database, has now been implemented in 68 of the 72 diplomatic missions and consular posts and should be completed.

The number of visas issued at the borders increased again in 2007, reaching over 8,300 visas - a 60% increase over 2006. Croatia should aim to minimise the issuing of visas at the border to exceptional cases. Currently there is limited equipment available at the borders to detect false or forged documents. The system for issuing visas is also still not unified or consistent. Croatia also needs to step up its preparations for the introduction of biometric identifiers in passports and travel documents.

There has been some progress with regard to **External borders and Schengen** the revised Integrated Border Management Action Plan was adopted in December 2007. The Coast Guard Law was adopted at the end of 2007, making the Navy responsible for the Coast Guard, and dividing responsibilities between the Coast Guard (outer waters), and Maritime Police (inner waters). An Inter-Ministerial Committee proposed a slight reduction in the number of Border Crossing-Points (BCPs) from 189 to 173, by eliminating some sea border crossing points, but no decision has been taken on this issue. The total staff of the Border Police has remained broadly unchanged at just over 5,000, and is well below the statutory staffing figure. A competition to hire 1,400 new police officers, of whom 800 were to be assigned to the Border Police, was held in May 2008. The installation of an encrypted communication system (Tetra) has been extended to the BCPs at the sea border, the islands and in Zagreb. The National Border Management Information System (NBMIS) is being deployed to some further BCPs, albeit at a slow pace owing to some technical problems, and it now covers nine BCPs.

Cross-border co-operation works well on a local level at all borders. Cross-border co-operation at national level continues to be constrained by the absence of formal bilateral agreements with countries at the future external border. Croatia signed a working arrangement with FRONTEX in April 2008 which provides a good basis for cooperation. Inter-service cooperation at the border should be strengthened.

Efforts to train Border Police staff have continued. However, the Border Police is still hampered by several shortcomings, such as a serious shortage of staff, limitations in general and specialised training, lack of equipment and poor infrastructure both at headquarters and at BCPs. In particular, further efforts are needed in establishing an overall management policy of BCPs, starting from a decision on their total amount and location. Croatia should also speed up the roll-out of the NBMIS system to cover the whole border.

As regards **judicial cooperation in criminal and civil matters**, there is only limited progress. The Agreement on Co-operation with EUROJUST was signed in November 2007, but it needs to be ratified by the Parliament. Further alignment as regards protection of personal data is needed before the agreement will be able to enter into force. Judicial cooperation is currently based on the conventional approach. This means, in practice, that recognition and enforcement of decisions by foreign courts has to go through the "exequatur" process at the Municipal or Commercial courts. The recognized decision is enforced according to Croatian law, which is slow and inefficient. Direct execution of foreign decisions is not possible. Croatia has not aligned with the Framework Decision on the execution in the EU of orders freezing property and evidence or with the Framework Decision on the application of mutual recognition of financial penalties. The Croatian legal order does not allow direct involvement between judicial authorities.

Furthermore, in Croatia every offence which has been committed in the territory of Croatia may be retried in Croatia, irrespective of a foreign judgment. This exception to *ne bis in idem* applies even if the offence was committed partly in Croatia and partly in a foreign State which has already delivered a judgment. The conditions to implement the Framework Decision on the European Arrest Warrant are not in place, as Croatia's Constitution does not allow it to extradite Croatian citizens. Croatia is a party to the Council of Europe Convention on the Transfer of Sentenced Persons (1983). It has not signed the Additional Protocol to the Convention (1997). Croatia has not yet acceded to the Hague Convention on Jurisdiction, applicable law, recognition, enforcement and co-operation in respect of parental responsibility and measures for the protection of children.

Regarding the status of victims in criminal proceedings, Croatian law is not aligned with the Framework decision in a number of areas. These include notifying the injured party that the perpetrator has been released after serving the sentence, acquiring testimonies by means of devices for picture and sound transmission (video and phone conferences), establishing a service for assistance to victims of criminal offences and as regards training of staff.

Some progress has been made as regards **police cooperation**. Since February 2008, a Croatian liaison officer has been stationed at Europol. Agreements on police cooperation have been signed with France and Austria. Croatia is actively involved in regional co-operation initiatives, including SECI. Reorganisation of the Criminal Police has started, but needs to be fully implemented.

However, within the Ministry of Interior decision making continues to be very complex and highly centralised. The human resources system of the police remains inadequate in terms of career development and resource management. There is no overall strategy or a Mission Statement for the Croatian police force.

While significant progress has been made, Croatia still needs to fully complete its institutional response to the issue of small arms and light weapons, by improving in particular the effectiveness of the arms transfer licensing system.

Some progress has been made in the area of **organised crime**. A high level inter-sectoral group within the police has adopted a national intelligence model, which in turn led to the preparation of the first-ever National Threat Assessment (NTA) which was adopted by the Ministry of Interior in late 2007 and has been shared with Europol. The NTA has been instrumental in the significant increase in intelligence reports and in developing police work in 2008. This signifies a marked shift of strategy and philosophy for the Croatian Police. An IT system for inter-Ministerial exchange of information has been completed (iCIS). A Protocol on Co-operation was concluded with the Ministry of Finance to enhance inter-agency cooperation, exchange of information, crime prevention and training. The co-operation protocol with USKOK, which entered into force in early 2007, is being implemented. The number of investigations is increasing. However, concrete results are needed in the fight against organised crime, which is a matter of concern. Improvements introduced are yet to lead to significant convictions. The police need to become more effective. Weaknesses in the judicial system also negatively affect the authorities' ability to effectively tackle organised crime.

Good progress has been made with regard to the **trafficking of human beings**. An Action Plan to combat trafficking in persons was adopted by the Government in December 2007. A new standard operating procedure (SOP) has been jointly elaborated by the Ministry of

Interior, the State Prosecutor, and Ministry of Social Services. A new protocol has also been drawn up and signed between the Ministry of Interior, the Ministry of Social Services and their NGO partners. Several workshops and awareness initiatives were organised over the period, including at regional level. Thirteen victims were discovered in 2007.

Limited progress can be reported in the fight against **terrorism**. Croatia signed the Council of Europe Convention on laundering, search, seizure and confiscation of the proceeds of crime and on the financing of terrorism, but this has yet to be ratified. Croatia needs to continue to strengthen its capacity in the fight against terrorism, in particular by continuing alignment of its legislation, strengthening its administrative capacity and developing inter-agency coordination.

Good progress has been made in the field of fight against **drugs**. Croatia signed the Agreement on Illicit Traffic by Sea, thus implementing Article 17 of the 1988 UN Convention against illicit traffic in narcotic drugs and psychotropic substances. The National Focal Point (NFP) became operational and delivered the first Annual Report to the European Monitoring Centre for Drugs and Drug Addiction (EMCDDA) in January 2008. Standards for therapeutic communities and a model for precursor control have been elaborated and adopted. A model for partnership co-operation between the national drug office and the districts has also been adopted. The Police recorded 7,900 criminal cases involving drugs in 2007 (which is commensurate with the level of each of the past 5 years).

Limited progress can be reported in the field of **customs co-operation**. In October 2007 Croatian Customs became a full member of MARINFO.

### *Conclusion*

Croatia has made some progress in this chapter, particularly as regards the fight against drugs and dealing with trafficking of human beings. However, significant efforts are needed in the area of external borders, in terms of human, financial and technical resources, in order to ensure that EU requirements are met upon accession. Also, concrete results are needed in the fight against organised crime, which is a matter of concern. Croatia needs to step up its efforts to ensure the necessary administrative capacity to implement and enforce the EU *acquis* upon accession.

### **4.25. Chapter 25: Science and research**

Good progress has been made in **research policy**. Two new bodies, the Strategic and Technology Council and the Council for the National Innovation System, were created in April 2008. This should allow for taking fully into account the innovation dimension in the research policy. Organisational changes at the level of the Ministry of Science have also taken place in view of strengthening administrative capacity. However, a fully transparent system for evaluation and monitoring of national research grants remains to be ensured in order to increase scientific excellence.

Good progress has been made on participation in the EC **Framework Programmes**. The grants awarded under the 7th Framework Programme for Research and Technological Development (FP7) continue to demonstrate Croatia's increased absorption capacity. However, full participation in the thematic collaborative cooperation has not yet been reached. The national contact points function well, but still lack administrative capacity. Croatia has confirmed its interest in becoming associated also to the Seventh Euratom Framework Programme.

With a view to further integration into the **European Research Area**, a “National 3 % Action Plan” was adopted in April 2008. This was a significant development. It includes a list of objectives and measures and envisages the establishment of a system of indicators in view of increasing investments into science and research to 3 % of the GDP. Steps have been taken to increase the administrative capacity for the implementation of the Action Plan. However, the entities responsible for implementation of the specific measures are not yet clearly defined. Steps have also been undertaken to ensure mobility of researchers. However, the share of the private sector in investment in research is low and there are not enough young people attracted to science.

#### *Conclusion*

Good progress has been made on this chapter, but further efforts remain necessary. The research capacity at national level needs to be strengthened which in turn will lead to increased participation under the FP7. Implementation of research policy and related action plans needs to be ensured in order to further integrate into the European Research Area.

#### **4.26. Chapter 26: Education and culture**

Good progress has been achieved in the field of **education, training and youth**. The education reform process has continued under the Education System Development Plan for 2005–2010. Croatia is participating in the EU Education and Training 2010 Work Programme. Additional efforts have been made in the development of a national qualifications framework (NQF). Implementation of the Bologna process in higher education has continued. The Law on primary and secondary Education, adopted in July 2008, incorporates the principle of non-discrimination in access to education for EU citizens and provisions for alignment with the *acquis* on education of children of migrant workers. A Strategy for Development of the Vocational Education System in the Republic of Croatia 2008–2013 was adopted in July 2008. As regards administrative capacity, staff and budgetary resources of the Agency for Vocational Education and Training and the Agency for Adult Education have been further increased. However, implementing legislation related to the Adult Education Act is still pending.

Good progress has been made in the preparation for the management of the Community Lifelong Learning and Youth in Action Programmes. The legal framework has been completed. Work plans for preparatory measures to be implemented in the second semester of 2008 and in 2009, including adequate training for the National Agency, have been submitted. The respective Accession Partnership priorities in the field of education, training and youth have been partially met.

Good progress can also be reported in the field of **culture**. Croatia has made efforts to facilitate deeper participation in the Culture Programme. Croatia has ratified the Memorandum of Understanding on its participation in the Europe for Citizens Programme.

#### *Conclusion*

Good overall progress has been made in the area of education, training, youth and culture. A good level of legal alignment has been achieved. Croatia should continue its efforts for preparing for the management of Life Long Learning and Youth in Action programmes.

#### 4.27. Chapter 27: Environment

There has been some progress with the **horizontal legislation**. Full transposition of the environmental impact assessment (EIA) and strategic environmental assessment (SEA) directives was achieved through the adoption of implementing regulations. Implementing legislation related to the rules for subsidies in environmental protection was also adopted. Directive on environmental liability is still not fully transposed. Enforcement of its existing provisions remains low. Work on the establishment of the Environmental Protection Information System (EPIS) is ongoing. The Act on Ratification of the Memorandum of Understanding on Croatia's participation in the Community Civil Protection Financial Instrument was adopted.

Some progress has been achieved in the area of climate change. An action plan for the implementation of the United Nations Framework Convention on Climate Change (UN FCCC) and its Kyoto protocol has been adopted. The national inventory reports on greenhouse gas (GHG) emissions for 2007 and 2008 have been submitted to the Convention Secretariat. Further work is required in the areas of GHG emission allowance trading, establishment of a national GHG registry and Croatia's participation in the EU Emissions trading scheme (EU ETS).

Good progress can be reported in the field of **air quality**. The Air Protection Act has been amended to ensure further alignment with the *acquis*. Further Protocols to the Long-Range Transboundary Air Pollution Convention (LRTAP) have been ratified. In addition, the National Air Quality Protection and Improvement Plan for the Period 2008-2011 has been adopted. Implementing legislation related to the use of organic solvents, fuel economy and CO<sub>2</sub> emissions of new passenger vehicles, as well as to establishment of zones and agglomerations by air category was also adopted. Work on the establishment of the national air quality monitoring and management system is ongoing. The programme for monitoring the quality of liquid fuels for 2008 has been adopted. The government continues to decide annually on the quantity of fuel on the market that does not comply with the prescribed quality standards. Transposition of the new *acquis* related to ambient air quality and cleaner air for Europe and emission ceilings related to atmospheric pollutants is required. Preparations in this area are progressing well.

There has been some progress with **waste management**. The Waste Act has been amended. Implementing legislation related to management of construction waste, categories and operating conditions for landfills and the management of sewage sludge in agriculture have been enacted. The Environmental Protection and Energy Efficiency Fund is financing the remediation of illegal landfills and sites containing hazardous waste. Ten further landfills have been remedied. Full alignment with the *acquis* in management of waste from extractive industries, hazardous waste and shipments and trans-boundary movement of waste is still required. Preparations in this area are advancing.

Little progress can be reported in the **water sector**. The Water Management Strategy has been adopted. The national monitoring programme is being prepared. A programme of monitoring bathing water quality has been launched. Adoption of the new Water Act, the new Water Management Financing Act and of implementing legislation is still pending. Preparations in this area require substantial efforts.

Some progress can be reported in the field of **nature protection** with the enactment of implementing legislation related to the establishment of the ecological network. This provides

the administrative framework for the designation of actual protected areas under Natura 2000. Designation of protected areas has not taken place yet. Additional efforts are needed in the sector to be in line with the *acquis*.

Some progress has been achieved in the area of **industrial pollution control and risk management**. Progress in the alignment with the integrated pollution prevention and control (IPPC) and Seveso II directives is advancing slowly. The Protocol on Pollutant Release and Transfer Registers has been ratified. The legal basis for the implementation of the pollutant register has been enacted but the register remains to start operating in practice. Activities on the reconstruction of one oil refinery in order to improve air and fuel quality are underway. Coordinated inspections of IPPC installations are starting to take place. Investments related to the alignment of industrial facilities with the air quality and large combustion plants directives need to be increased. The clean-up of sites contaminated with asbestos is continuing. Significant efforts will be required to align with the *acquis* and build up administrative capacity in this area.

Good progress can be reported on **chemicals** and **genetically modified organisms (GMOs)**. The Chemicals Act has been amended to ensure further alignment with the *acquis* and the law implementing REACH has been enacted. Implementing legislation related to labelling and packaging, and sorting of chemicals has been enacted. Further alignment with the *acquis* has been achieved by amending the Biocides Act. The National Chemicals Strategy has been adopted. In relation to GMOs, implementing legislation has been adopted related to the keeping of the Register of GMOs and risk assessment for placing GMOs on the market. Preparations in these areas are progressing well.

Little progress can be reported in the **noise** sector. Preparations in this area are still at an early stage.

There has been progress related to **forestry**. Implementing legislation related to data collection, observation and registers related to forest fires has been enacted. Preparations in this area are advancing.

Progress has been made to increase **administrative capacity**. The Action plan for setting up the necessary administrative capacities at national, regional and local level and required financial resources for implementing the *acquis* has been adopted. However, capacity for the implementation of the *acquis* remains overall weak, particularly at the local level. There is a particular need for training in the implementation of new legislation to both the administration and economic operators which will be obliged to comply with the new legislation. Due consideration should also be given to improving the coordination mechanisms between all institutions/bodies involved in environmental protection.

### *Conclusion*

Overall, good progress has been achieved in the environment chapter, especially in the areas of air quality, chemicals and GMOs. Considerable efforts will be needed to further align with and implement the *acquis* in the water, industrial pollution control and risk management, climate change and horizontal sectors. Substantial efforts will be needed in the forthcoming period to meet the requirements of the environment chapter especially as regards investments.

#### 4.28. Chapter 28: Consumer and health protection

There has been some progress in the field of **consumer protection**. As regards administrative capacity, the Consumer Protection Department in the Ministry of Economic Affairs, Labour and Entrepreneurship is being reorganised into four sections and staff being increased up to 17. In February 2008, the National Consumer Protection Council became an advisory body to the Government. The Council comprises representatives of state administrative bodies in charge of consumer protection, representatives of Croatian Chamber of Economy, Croatian Chamber of Trades and Crafts, consumer protection associations and independent consumer protection specialists which are appointed for four years. Government funding for consumer organisations has further increased and support for regional counselling centres has continued. Activities for raising awareness on consumer protection have continued in the context of the 2007 Year of Consumer Education in Croatia. As for consumers' access to justice, the mechanisms for out-of-court settlement of consumer disputes are not sufficiently developed or known by consumers. As a consequence, they treat only a small percentage of possible consumer protection cases. Preparations in this field are advanced.

Some progress can be reported in the field of *product-safety related issues*. RAPEX contact point has been established within the State Inspectorate. The underlying network of local and sectoral authorities responsible for market surveillance as well as their interconnection is under construction. Legal alignment of the Croatian general product safety legislation with the *acquis* is at an advanced stage. However, coordination between the RAPEX central contact point and local authorities as well as due enforcement of measures on general product safety remain outstanding. Preparations in this field are well on track.

Good progress has been made in the area of *non-safety related issues*. Amendments to the Civil Obligation Act were adopted in March 2008 aiming at completing legal alignment in the fields of the sale of consumer goods and associated guarantees as well as package travel. However, shortcomings remain as regards legal alignment. In particular, an effective enforcement mechanism against unfair terms in consumer contracts is outstanding. Preparations in this field are well advanced.

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

Good progress has been made in the area of *tobacco*. The WHO Framework Convention on Tobacco Control was ratified in March 2008. Legislation was adopted in October 2008 aimed at completing legal alignment in the fields of tobacco advertising and tobacco products. This is a key element for the accession negotiations on this chapter. Preparations in this field are reaching completion.

Some progress has been made in the field of *communicable diseases*. The Act on the protection of the population against communicable diseases was amended in September 2008. A manual on definitions of infectious diseases to be reported was published by the Croatian National Institute of Public Health in December 2007. Contact persons and institutions for the Early Warning and Response System (EWRS) have been appointed. Preparations in this field are well advanced.

Some progress can be reported in the area of *blood*. As regards restructuring of blood transfusion services, a basic transfusion network is being established since December 2007, and the number of blood collection and processing units is being reduced from 21 to 9. Provision of software and hardware to all blood transfusion centres has started. However,

administrative capacity is not yet sufficiently developed, especially in the Ministry of Health and in inspection departments, a serious adverse events and reactions reporting system is not operational, and quality management of all blood transfusion centres is not ensured. Preparations in this field are well advanced.

Limited progress can be reported in the field of *tissues and cells*. Legal alignment in the field of reproductive cells is still outstanding. This is a key element for the accession negotiations on this chapter. Administrative capacity is not yet sufficiently developed, especially in the Ministry of Health and in inspection departments. A serious adverse events and reactions reporting system is not in place. Facilities for handling tissues and cells have not yet been upgraded, restructured and licensed according to the EU technical requirements. Preparations in this field are underway.

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

Good progress has been made in the field of colorectal *cancer* screening, and legislation has been adopted aiming at completing legal alignment in the area of electromagnetic fields. A focal point for the area of non-ionising radiation has been appointed in the Ministry of Health. Preparations in these areas are well on track.

### *Conclusion*

Overall, some progress has taken place in the area of consumer and health protection. A good level of legal alignment has been reached. However, legislation in the fields of consumer product safety and public health, in particular on reproductive tissues and cells, is not yet in line with the *acquis*. Continued efforts are required, also to implement and enforce legislation effectively. In the area of consumer product safety, Croatia should focus on establishing a proper interconnection between RAPEX central contact point and competent local and sectoral authorities. In the field of public health, attention should be paid to adequate administrative capacity, serious adverse events and reactions reporting systems as well as upgrading and restructuring of facilities for handling blood, tissues and cells in order to meet EU technical requirements.

### **4.29. Chapter 29: Customs union**

Good progress has been made in the area of **customs legislation**. The Regulation on the customs tariff for 2008 entered into force in January 2008 and aligned the Croatian tariff with the 2008 Combined Nomenclature. Duty relief applies to all pharmaceutical products. The Act amending the Customs Act and its implementing regulation entered into force in July 2008 and aligned the provisions regulating non-preferential origin, the guarantee in transit procedures, entry of debt in accounts, the time limits for payment of customs debt and deferred payment and other privileges. The list of narcotic drugs, psychotropic substances and plants was adopted in April 2008 and aligned with the classification laid down by the *acquis*. Most of the fees charged by the customs authorities have been abolished; the others will remain in force until 31 December 2008.



Some discrepancies with the *acquis* remain in allocation of quotas, duty relief, duty exemptions for passengers and the internal transit arrangements. Overall, alignment of the customs rules with the *acquis* is well on track.

Good progress can also be reported on **administrative and operational capacity**. The internal audit department has been reinforced and now has a staff of 17 officials; relevant auditing procedures have been adopted, including for compulsory reporting and implementation of recommendations emerging from the audits. The IT-based centralised risk analysis system was rolled out to all customs offices. As it is still in its initial phase, it needs continuous upgrading to keep it effective. The strengthening of the audit department, combined with deployment of the centralised system of risk analysis and with improved post-clearance controls, has ensured more uniform application of customs procedures across all customs offices, which was a requirement in the accession negotiations. Work has continued, albeit with some delays, on computerisation and interconnectivity, another key requirement in the accession negotiations. The Croatian customs administration still has very limited in-house capacity to guarantee the continuity of its IT services and remains heavily dependent on external companies. Areas where progress was uneven were the fight against corruption, with a very limited number of cases reported, and detection of infringements of intellectual property, illegal arms and protected species, which remained weak and concentrated in specific customs offices. Overall, in the area of administrative and operational capacity, Croatia has consistently addressed its targets and priorities.

### *Conclusion*

Croatia has made good progress on legislative alignment as well with its administrative capacity by developing the conditions for uniform application of customs rules. Progress has also continued in the area of IT interconnectivity. Efforts need to continue in the remaining areas of legislative alignment, to fight against corruption, to create the conditions for effective implementation of customs rules and to make further progress on IT interconnectivity.

### **4.30. Chapter 30: External relations**

There has been good progress in the field of the **common commercial policy**. In May 2008, Croatia adopted an action plan for the remaining preparations in terms of legislation and bringing international agreements into conformity with the *acquis* which is a key element for the accession negotiations in this chapter. This action plan also foresees continuous training in all relevant areas. A revised Trade Act preparing for the application of the common commercial policy was adopted in July 2008. Croatia needs to continue to cooperate and coordinate closely with the Commission and to align with the policies and positions of the EU towards third countries and within international organisations, particularly the *World Trade Organisation*.

With regard to export insurance, Croatia has further aligned its legislation with the *acquis* and published rules on State aid for short-term export loans insurance. In relation to *dual-use goods*, Croatia continued to align to with the revised list of dual-use items and technology. Croatia simplified the procedure for issuance of export and import permits for dual-use goods, strengthened provisions on the fight against illicit exports and started various training activities in order to enhance administrative capacity. It needs to continue to work on the remaining adjustments and on further enhancing its administrative, control and reporting capacity for dual-use goods. Overall, preparations in the area of the common commercial policy are well on track.

In the area of **bilateral agreements with third countries**, Croatia actively participates in the work of the Central European Free Trade Agreement (CEFTA), which entered into force for all signatory parties in November 2007. Croatia signed a trade and cooperation agreement as well as an investment agreement with Vietnam. Croatia also signed bilateral investment agreements with Lithuania and Azerbaijan. Croatia has analysed all its existing agreements, in particular all investment and trade-related agreements in order to bring them, upon accession, into conformity with the *acquis*. Croatia will now need to continue implementing the Action plan as adopted to this effect. Preparations in this area are well advanced.

Some progress can be reported on **development policy** and **humanitarian aid**. A new department responsible for developmental cooperation was established within the Ministry of Foreign Affairs and European Integrations in November 2007. Croatia currently does not collect statistics on development and humanitarian aid in line with OECD/ODA standards, however, progress has been made towards meeting the standard. Croatia will need to establish the required legal framework in this area. Generally, preparations in this area are well advanced.

### *Conclusion*

Croatia has made further progress in this chapter. Provided Croatia continues preparations as scheduled and improves its administrative capacity, it should be able to apply the *acquis* and participate in the common commercial policy upon accession. Continued efforts are also needed in the areas of development policy and humanitarian aid.

## **4.31. Chapter 31: Foreign, security and defence policy**

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

Concerning **Common Foreign and Security Policy (CFSP)**, Croatia has continued to systematically align itself with EU common positions, declarations, and statements. With regard to administrative capacity, further training activities have taken place in order to develop future capacity to work with the EU CFSP structures. The post of "Political Director" in the Ministry for Foreign Affairs and European Integration remains to be formally established.

In the area of *restrictive measures*, legislative alignment remains advanced. However, a continued strengthening of interagency coordination is required.

As regards *non-proliferation*, the legislative framework for arms control is satisfactory. However, there remains a need to further strengthen implementation and enforcement capacity as well as transparency of arms related information. A comprehensive National Strategy for the Control of Small Arms and Light Weapons remains to be adopted.

With regard to the *cooperation with international organisations*, Croatia has, as a member of the UN, OSCE and the Council of Europe, been fully involved in the policy making of these organisations. Since January, Croatia has been a non-permanent member of the UN Security Council. *As regards the International Criminal Court, see Political criteria – Regional issues and international obligations.*

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

Croatia has remained committed to the development of the **European Security and Defence Policy (ESDP)** including through further training and administrative capacity building. Croatia has made further commitments to actively participate in civilian operations within the ESDP in order to strengthen the EU's crisis management capacity, in particular in Kosovo<sup>10</sup>. Croatia has continued to take part in international peacekeeping efforts and has increased to 41 its personnel currently participating in nine UN peacekeeping missions. Moreover, 200 Croatian armed forces personnel are deployed in Afghanistan (ISAF).

### *Conclusion*

Croatia has continued to make progress in this chapter. Overall, Croatia has reached a good level of alignment in the area of Foreign, Security and Defence Policy. In order to be fully prepared for accession, Croatia needs to strengthen implementation and enforcement of arms control including transparency of arms-related information, and to further improve capacity for full implementation of CFSP-ESDP.

### **4.32. Chapter 32: Financial control**

Good progress can be reported in the area of **public internal financial control (PIFC)**.

As regards the regulatory framework, in November 2007 the Croatian government adopted an independent development strategy on PIFC for local and regional self-government units. A Code of Ethics for Internal Auditors was approved in January 2008. Furthermore, the Internal Auditors' Charter and the rulebooks on internal audit of budget users and on public financial management and control were updated in March 2008. In July 2008 the new Budget Law was adopted, removing inconsistency with provisions of the PIFC law. Furthermore, the financial inspection was made compatible with the PIFC approach with the new Regulation on Budgetary Control in July 2008.

As regards the institutional framework, the work and responsibilities of the Central Harmonisation Unit (CHU) have been further streamlined and enhanced. However, the capacity of the CHU and all budget users at central and local levels needs to be strengthened and there is a need for more sustainable training arrangements that would allow the CHU to better focus on PIFC methodology development and co-ordination.

There has been little progress in the area of **external audit**, a key element for the accession negotiations in this chapter. Although the new Strategic Plan for 2008-2012 was adopted in December 2007 and the relevant work program for 2008 is being implemented together with continuous training for external auditors, the capacity of the SAO to perform audit activities needs to be enhanced, especially in the field of auditing of EU funds. Croatia also has to make appropriate proposals on how to comply with the need to consolidate the independence of the SAO.

Some progress has been made on **protection of the EU's financial interests**, a key element for the accession negotiations in this chapter. Although two regulations were adopted in March 2008, including provisions on irregularity reporting on EU funds and on the scope of

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<sup>10</sup> Under UN Security Council Resolution 1244

the work of the Budget Supervision Sector within the State Treasury of the Ministry of Finance, acting as the AFCOS, the above-mentioned legal framework should be further improved to cover the overall mechanism of the anti-fraud coordination system to be established in the country. In this regard, an Anti-Fraud Strategy together with a detailed Action Plan covering the specific role and responsibilities of all bodies involved in the system is required. The administrative capacity of the AFCOS needs to be further enhanced, especially with regard to coordinating procedures for recovery of EU funds and their role in SF management after accession. Public awareness of anti-fraud issues should be raised, based on establishment of an efficient system for fraud prevention, detection and follow-up.

Good progress can be reported on **protection of the euro against counterfeiting**, which is a key element for the accession negotiations in this chapter. In November 2007, the Croatian National Bank adopted a decision on medals and tokens similar to euro coins which lays down the procedures for handling suspicious banknotes and coins and for protection against counterfeiting. It also signed cooperation agreements on prevention of counterfeiting of the euro with the Ministry of the Interior, the European Central Bank and the European Commission (OLAF). In March 2008, the Croatian National Bank endorsed the Decision on establishment of the National Counterfeit Centre, the National Analysis Centre and the National Coin Analysis Centre that will enter into force on 1 March 2009. However, further efforts are needed to ensure efficient implementation of the regulations and to strengthen the capacity of the new centres.

### *Conclusion*

Overall, some progress has been made by Croatian authorities towards fulfilling their obligations under this chapter. Continued efforts are needed to establish a strong and adequate PIFC system, covering the institutional framework. In particular, improvements are still needed in the legal basis for the functional independence of the SAO and in anti-fraud strategy. Moreover, the overall capacity of the CHU and of all budget users at central and local levels needs to be further enhanced.

### **4.33. Chapter 33: Financial and budgetary provisions**

There has been some progress on this chapter. The unit for the coordination and management of the **own resources** system in the Ministry of Finance is gradually developing its capacity to play the coordination role required of it from accession. The relevant institutions responsible for the system of own resources have been defined and an informal working group comprising representatives of all key institutions has been established.

Although the *acquis* in this area does not require transposition, Croatia will need to build the capacity of its coordination unit, further develop cross-institutional cooperation and adopt implementing rules so as to ensure from accession the correct calculation, collection, payment and control of own resources and reporting to the EU in line with the *acquis*. As regards traditional own resources, A&B accounts and OWNRES-reporting need to be developed, a system for sugar levies and for writing-off irrecoverable debts introduced and post clearance control improved.

The capacity to calculate the VAT base, especially the Weighted Average Rate, required significant strengthening. The concrete tasks, responsibilities and relations of key institutions in the own resources system require further streamlining through the development and implementation of working procedures, guidelines and manuals.

For the GNI resource, further implementation of the ESA 95 concept is needed, together with enhancing the exhaustiveness of national accounts and GNI calculations.

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

### *Conclusion*

There has been some progress in this chapter, notably the development of a coordination structure for own resources. Overall, Croatia has reached a good level of alignment with and capacity to implement the *acquis*. Administrative capacity of the coordination structure needs to be further built up and rules and procedures for implementing own resources put in place.

## STATISTICAL ANNEX

### STATISTICAL DATA (as of 29 September 2008)

#### Croatia

<b>Basic data</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Population (thousand)		4 537e	4 527e	4 498e b	4 439e	4 445e	4 443e	4 442e	4 444e	4 443e	4 441e
Total area of the country (km <sup>2</sup> )	1)	56 542	56 542	5 498e	56 542	56 542	56 594	56 594	56 594	56 594	56 596
<b>National accounts</b>											
	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Gross domestic product (GDP) (million national currency)	2)	137 604	141 579	152 519	165 640	181 231	198 422	214 983	231 349	250 590	275 078
GDP (million euro)	2)	19 272	18 677	19 955	22 138	24 448	26 216	28 677	31 263	34 221	37 497
GDP (euro per capita)	2)	4248e	4125e	4437e	4987e	5501e	5901e	6456e	7035e	7702e	8443e
GDP (in Purchasing Power Standards (PPS) per capita)		7 400e	7 400e	8 200e	8 600e	9 300e	9 800e	10 600e	11 100e	11 700e	:
SI: GDP (in PPS per capita, EU-25=100)		42.0e	40.0e	41.3e	41.8e	43.7e	45.6e	47.0e	47.9e	48.1e	:
SI: Growth rate of GDP (national currency, at constant prices, % change on previous year)	2)	2.5	-0.9	2.9	4.4	5.6	5.3	4.3	4.3	4.8	5.6
SI: Employment growth (national accounts, % change on previous year)		-3.0	-3.3	4.0	-5.4	4.2	0.6	:	:	:	:
Labour productivity growth: GDP growth per person employed (% change on previous year)		5.8	2.6	-1.2	10.4	1.6	4.7	:	:	:	:
SI: Unit labour cost growth (national accounts, % change on previous year)		0.9	4.2	-3.3	-5.3	1.5	2.4	:	:	:	:
SI: Labour productivity (GDP in PPS per person employed, EU-25=100)		51.8e	52.1e	50.5e	55.3e	55.5e	57.5e	58.4	59.4e	59.1e	:
Gross value added by main sectors (%)											
Agriculture	2)	9.4	9.6	8.8	9.0	8.7	7.0	7.5	7.3	7.1	6.8
Industry	2)	25.0	24.6	24.7	24.3	23.0	22.8	23.4	23.8	23.5	23.3
Construction	2)	6.6	5.3	4.6	4.9	5.3	6.3	6.6	6.5	6.8	6.8
Services	2)	59.0	60.4	61.9	61.8	63.1	63.9	62.5	62.4	62.6	63.0
Final consumption expenditure, as a share of GDP (%)	3)	85.5	85.4	84.9	82.1	81.9	79.7	78.3	77.4	76.1	75.9
Households and NPISH, as a share of GDP (%)	3)	60.1	58.9	60.1	60.1	60.4	58.8	57.9	56.9	56.0	55.8
General government, as a share of GDP (%)	3)	25.4	26.5	24.8	22.0	21.6	21.0	20.4	20.5	20.1	20.1
Gross fixed capital formation, as a share of GDP (%)	2)	23.3	23.3	21.8	22.3	24.3	28.6	28.1	28.1	29.9	30.0
Changes in inventories, as a share of GDP (%)	2)	0.7	-0.3	-1.6	1.6	4.8	2.5	2.5	2.9	2.9	2.8
Exports of goods and services, relative to GDP (%)	2)	39.6	40.9	47.1	48.4	45.3	47.1	47.5	47.1	47.9	47.7
Imports of goods and services, relative to GDP (%)	2)	49.2	49.3	52.3	54.5	56.4	57.9	56.4	55.5	56.8	56.3
<b>Industry</b>											
	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Industrial production volume index (2000=100)	4)	99.8	98.3	100.0	106.0	111.8	116.3	120.6	126.7	132.4	139.8
<b>Inflation rate</b>											
	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
SI: Consumer price index (CPI), (total, % change on previous year)		:	4.0	4.6	3.8	1.7	1.8	2.1	3.3	3.2	:
<b>Balance of payments</b>											
	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Balance of payments: current account total (million euro)		:	-1 429	-568	-821	-2 099	-1 889	-1 434	-1 976	-2 696	-3 226
Balance of payments current account: trade balance (million euro)		:	-3 102	-3 492	-4 595	-5 958	-6 971	-6 724	-7 518	-8 344	-9 434

Balance of payments current account: exports of goods (million euro)	:	4 138	4 977	5 327	5 296	5 575	6 607	7 220	8 464	9 193
Balance of payments current account: imports of goods (million euro)	:	7 240	8 469	9 923	11 253	12 546	13 331	14 738	16 808	18 626
Balance of payments current account: net services (million euro)	:	1 545	2 470	3 303	3 285	4 933	4 769	5 318	5 710	6 309
Balance of payments current account: net income (million euro)	:	-465	-505	-628	-578	-1 095	-670	-959	-1 170	-1 144
Balance of payments current account: net current transfers (million euro)	:	594	959	1 099	1 152	1 245	1 192	1 184	1 107	1 043
of which government transfers (million euro)	:	-123	25	65	32	71	3	10	-9	-17
Foreign Direct Investment (FDI) in the reporting economy (million euro)	:	1 363	1 141	1 467	1 138	1 762	950	1 468	2 745	3 597

<b>Public finance</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
General government deficit/surplus, relative to GDP (%)	5)	:	-7.1	-7.5	-6.8	-4.9	-6.2	-4.8	-4.0	-3.0	-2.6
SI: General government debt, relative to GDP (%)	:	33.0	40.1	41.3	39.8	40.4	42.2	44.0	40.9	38.1	

<b>Financial indicators</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Gross foreign debt of the whole economy, relative to GDP (%)		47.6	54.5	61.4	61.4	61.9	75.8	80.0	82.4	85.5	87.8
Gross foreign debt of the whole economy, relative to total exports (%)		119.4	133.0	130.2	125.9	136.1	151.3	161.0	168.6	172.2	179.2
Money supply: M1 (banknotes, coins, overnight deposits, million euro)		1 846	1 805	2 373	3 216	4 148	4 432	4 505	5 263	6 606	7 901
Money supply: M2 (M1 plus deposits with maturity up to two years, million euro)		:	:	:	:	:	:	:	:	:	:
Money supply: M3 (M2 plus marketable instruments, million euro)		:	:	:	:	:	:	:	:	:	:
Total credit by monetary financial institutions to residents (consolidated) (million euro)		9 131	8 587	9 483	11 891	15 119	16 526	18 417	22 836	27 274	30 863
Interest rates: day-to-day money rate, per annum (%)		10.3	9.3	6.9	3.0	1.3	4.3	5.9	3.4	2.4	5.6
Lending interest rate (one year), per annum (%)		20.1	20.9	20.6	19.5	16.5	15.0	14.4	13.1	12.1	12.1
Deposit interest rate (one year), per annum (%)		9.6	9.5	8.2	6.6	5.4	3.8	3.8	3.9	4.0	4.2
euro exchange rates: average of period - 1 euro = ... national currency	6)	7.140	7.580	7.643	7.482	7.413	7.569	7.497	7.401	7.325	:
Effective exchange rate index (2000=100)		:	95.4	100.0	98.7	96.5	93.7	90.4	89.2	:	:
Value of reserve assets (including gold) (million euro)		2 400	3 013	3 783	5 334	5 651	6 554	6 436	7 438	8 725	9 307

<b>External trade</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Trade balance: all goods, all partners (million euro)		:	:	:	:	-6 139	-7 071	-6 901	-7 880	-8 853	-9 832
Value of exports: all goods, all partners (million euro)		:	:	:	:	5 188	5 439	6 454	7 069	8 252	8 855
Value of imports: all goods, all partners (million euro)		:	:	:	:	11 327	12 510	13 354	14 950	17 105	18 686
Terms of trade (export price index / import price index)	7)	:	:	:	-4.0	3.6	0.4	11.3	-15.3	8.2	4.2
Share of exports to EU-27 countries in value of total exports (%)		:	:	:	:	66.1	68.3	65.8	63.3	64.3	60.9
Share of imports from EU-27 countries in value of total imports (%)		:	:	:	:	71.9	73.3	71.0	67.9	67.2	64.8

<b>Demography</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Natural growth rate: natural change (births minus deaths) (per 1000 inhabitants)		-1.2	-1.5	-1.5	-1.9	-2.4	-2.9	-2.1	-2.1	-2.0	-2.4
Net migration rate: immigrants minus emigrants (per 1000 inhabitants)	8)	9.8	4.1	5.3	3.8	1.9	2.7	2.6	1.9	1.6	1.3
Infant mortality rate: deaths of children under one year of age per 1000 live births		8.2	7.7	7.4	7.7	7.0	6.3	6.1	5.7	5.2	5.6
Life expectancy at birth: male (years)		:	:	70.5	71.1	71.2	71.4	72.0	71.8	72.5	72.3
Life expectancy at birth: female (years)		:	:	77.8	78.1	78.3	78.4	79.0	78.8	79.3	79.2

<b>Labour market</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Economic activity rate (15-64): share of population aged 15-64 that is economically active (%)	9)	62.8	62.6	62.2	62.2	62.9b	62.4	63.7	63.3	62.6	63.2
SI: Employment rate (15-64): share of population aged 15-64 that is in employment (%)	9)	55.3	53.2	51.3	51.8	53.4b	53.4	54.7	55.0	55.6	57.1
Share of male population aged 15-64 that is in employment (%)	9)	61.7	59.0	57.4	59.0	60.5b	60.3	61.8	61.7	62.0	64.4
Share of female population aged 15-64 that is in employment (%)	9)	49.4	47.8	45.5	44.9	46.7b	46.7	47.8	48.6	49.4	50.0
SI: Employment rate of older workers (55-64): share of population aged 55-64 that is in employment (%)	9)	25.6	25.9	24.2	23.7	24.8b	28.4	30.1	32.6	34.3	35.8
Employment by main sectors (%)											
Agriculture	9)	16.5	16.7	11.7	15.6	15.5b	16.9	17.0	17.3	14.2	13.0
Industry	9)	23.5	23.9	22.7	23.1	22.6b	22.1	21.4	20.5	20.9	21.8
Construction	9)	6.7	6.6	5.9	6.3	7.2b	8.1	8.2	8.2	8.4	8.8
Services	9)	53.2	52.8	59.6b	55.0	54.6b	52.8	53.2	54.0	56.3	56.4
SI: Unemployment rate: share of labour force that is unemployed (%)	9)	11.7	14.5	17.0	16.3	14.7b	14.1	13.6	12.6	11.1	9.6
Share of male labour force that is unemployed (%)	9)	10.6	13.5	15.9	14.4	13.2b	12.8	12.0	11.6	9.8	8.4
Share of female labour force that is unemployed (%)	9)	12.9	15.7	18.2	18.7	16.5b	15.6	15.6	13.8	12.7	11.2
Unemployment rate of persons < 25 years: share of labour force aged <25 that is unemployed (%)	9)	31.0	39.2	43.1	41.7	34.4	35.8	33.8	32.0	28.8	24.0b
SI: Long-term unemployment rate: share of labour force that is long-term unemployed (%)	10)	5.4	7.3	9.1	10.1	8.9b	8.4	7.3	7.4	6.7	5.9

<b>Social cohesion</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Average nominal monthly wages and salaries (national currency)	11)	4 131.0	4 551.0	4 869.0	5 061.0	5 366.0	5 623.0	5 985.0b	6 248.0	6 634.0	7 047.0
Index of real wages and salaries (index of nominal wages and salaries divided by the CPI) (2000=100)	11)	92.4	98.4	100.0	99.2	103.2	106.1	112.2b	113.4	116.6	120.4
SI: Early school-leavers: share of population aged 18-24 having not completed upper secondary education and not currently in education or training (%)	9)	:	:	:	:	8.3	8.4	6.2	4.8	5.1	3.9b

<b>Standard of living</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Number of passenger cars per 1000 population		222.2	233.5	254.1	269.3	280.2	291.3	301.3	311.7	323.4	336.1
Number of subscriptions to cellular mobile telephone services per 1000 population		39.3	79.3	251.2	389.9	520.9	571.4	638.7	821.7	989.9	1 135.0

<b>Infrastructure</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Density of railway network (lines in operation, per 1000 km <sup>2</sup> )		47.8	47.8	47.8	47.8	47.8	47.7	47.7	47.7	47.7	47.7
Length of motorways (thousand km)		0.3	0.4	0.4	0.4	0.5	0.6	0.7	0.8	0.9	1.0

<b>Innovation and research</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
SI: Spending on human resources (public expenditure on education) relative to GDP (%)		:	4.2	4.5	4.2	4.3	4.5	:	:	:	:
SI: Gross domestic expenditure on research & development, relative to GDP (%)		:	1.0	1.2	1.1	1.1	1.1	1.2	1.0	0.9	:
SI: Percentage of households who have Internet access at home (%)		:	:	:	:	:	:	:	:	:	:

<b>Environment</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
SI: Total greenhouse gases emissions, CO2 equivalent (tons, 1990=100)		78.1	81.3	81.2	84.9	88.7	93.8	94.6	:	:	:
SI: Energy intensity of the economy (kg of oil equivalent per 1000 euro GDP 2004)		346.0	345.8	330.1	321.9	330.3	321.1	308.3	297.6	285.9	:
SI: Share of renewable energy in electricity consumption (%)		38.3	45.1	40.0	42.7	33.9	29.4	41.0	58.1	60.5	:
SI: Road freight transport as a share of total inland freight transport (modal split of freight transport) (%)		:	:	:	75.9	76.4	76.2	76.6	76.0	74.8	74.0



<b>Energy</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Primary production of all energy products (thousand TOE)		3 983	3 570	3 562	3 730	3 689	3 727	3 852	3 781	4 128	:
Primary production of crude oil (thousand TOE)		1 825	1 394	1 328	1 232	1 200	1 138	1 079	1 017	985	:
Primary production of hard coal and lignite (thousand TOE)		31	9	0	0	0	0	0	0	0	:
Primary production of natural gas (thousand TOE)		1 282	1 267	1 355	1 642	1 732	1 789	1 796	1 854	2 204	:
Net imports of all energy products (thousand TOE)		3 991	4 427	4 174	4 166	4 967	4 985	5 090	5 234	4 866	:
Gross inland energy consumption (thousand TOE)		8 037	7 959	7 819	7 959	8 624	8 828	8 842	8 902	8 948	:
Electricity generation (thousand GWh)		10.9	12.2	10.7	12.2	12.3	12.7	13.3	13.1	13.0	12.5

<b>Agriculture</b>	Note	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Agricultural production volume index of goods and services (producer prices, previous year=100)		110.1	98.8	88.7	108.5	107.7	84.1	111.9	91.3	104.4	96.0
Total utilised agricultural area (thousand hectare)	12)			1 169	1 178	1 181	1 200	1 201	1 185b	1 169	1 201
Livestock: cattle (thousand heads, end of period)		443	438	427	438	417	444	466	471	483	467
Livestock: pigs (thousand heads, end of period)		1 166	1 362	1 234	1 234	1 286	1 347	1 489	1 205	1 488	1 348
Livestock: sheep and goats (thousand heads, end of period)		510	567	608	632	677	673	848b	931	783	738
Production and utilisation of milk on the farm (total whole milk, thousand tonnes)		653	641	626	674	716	686	708	813	870	883
Crop production: cereals (including rice) (thousand tonnes, harvested production)		3 209	2 881	2 312	2 829	3 080	2 014	3 067	3 039	3 034	2 534
Crop production: sugar beet (thousand tonnes, harvested production)		1 233	1 114	482	965	1 183	678	1 260	1 338	1 560	1 583
Crop production: vegetables (thousand tonnes, harvested production)		:	:	196	208	218	154	150	286	304	281

SI:Structural Indicator

e: estimate

f: forecast

p: provisional

b: break in serie

1. Land area.
2. For 2005-2007, data is based on quarterly values.
3. For 2005-2007, data is based on quarterly values; NPISH is not included.
4. Gross series; include NACE Sections C to E.
5. GFS 1986 basis. Privatisation revenues are excluded and reclassified to the financing of the balance.
6. 1999-2006, source: Eurostat.
7. Calculated on the basis of exports and import values expressed in US dollars; break in series in 2004: change in methodology as of 1 January 2004.
8. Total number of migrants includes Croatian citizens and permanently resident foreigners who reported/unreported their place of permanent residence in the Republic of Croatia at the Ministry of Interior.
9. For 1998-2001, data refer to the second half of the year; in 2007, data refer to the annual average of quarterly data.
10. For 1998-2001, data refer to the second half of the year and long-term unemployment refers to thirteen months or more; in 2007, data refer to the third quarter.
11. For the period 1998-2003, the persons employed in crafts, trades and as free-lances, as well as in the police and defense-related activities are excluded; from 2004 onwards the number of persons employed in the police and defense-related activities are included.
12. Since 2005, data is obtained by using the interview method based on a selected sample.