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DEMOCRACY AND THE RULE OF LAW

The parliamentary and presidential elections held in October 2010 proved inconclusive. The government in the Federation of Bosnia and Herzegovina (FBiH) only approved the FBiH Parliament on 17 March 2011. However, the government was formed without the main Bosnian Croat party (HDZ BiH), who is now calling local authorities not to obey the Federation Government. The situation at the state level is unresolved and the Parliament has been not able to form a government. The National Assembly of Republika Srpska keeps defying the state level institutions and was until recently considering holding a referendum on the state-level war crimes court and on the “anti-constitutional laws and activities of the High Representative in Bosnia”.

The deteriorating political situation and continuing fiscal difficulties will have a negative impact on the timing and feasibility of public administration reforms. Because the underlying reasons are political rather than administrative, current public administration reform efforts are likely to have little impact on real administrative performance.

Democracy

The underlying reasons for the major deficiencies in the governance system are the lack of respect for fundamental democratic tenets (individual political rights versus ethnic or group-based) and the disrespect of the law and existing institutions by major actors, whether they be parliament, the executive or the judiciary, or civil society and its organisations. This is a matter of democratic and legal culture. The international community, which itself sometimes overrides constitutional constraints in order to pursue political objectives, should cease promoting legal and managerial solutions that do not fit the stage of development of existing institutions or the constitution. Some partial solutions to problems may undermine the rule of law and render current tensions more acute. For example, the international community exercised strong political pressure in presenting the need for a unified police force as a European standard, when it is not and when the BiH constitution allows the entities to create their own particular police corps, whereas the common institutions do not have that competence under the Dayton Peace Agreement.

Rule of law

The limited extent to which the public governance system puts the rule of law into practice remains a serious matter of concern.¹

The poor quality of legislation is still a common problem. Major reasons for insufficient quality of legislation include: a fragmented governance system with multiple veto points; deficient law drafting capacity in ministries and administrative bodies; inadequate consultation with regulated communities; poor translations of European laws and adoption of laws drafted by international consultants from alien contexts

¹ The rule of law includes, for the purpose of this report, a set of principles such as:

1. The separation of powers between the judicial, executive and legislative branches of government,
2. Compliance with the law by government and the proper functioning of the judiciary, and
3. The consistent application of fair procedures by the administration.

resulting in a system rich in written laws but poor in laws that effectively regulate in accordance with their intended purpose; inadequate attention to implementation issues during drafting; constrained potential for parliament to scrutinise government proposals adequately.

The international community should better co-ordinate its efforts to ensure a coherent style throughout the legal framework, in order to make it comprehensive, consistent and transparent. The legal tradition derives from continental European law; there is now a mixture of legal styles from various continental as well as common law traditions. The incompatibilities amongst different laws and legal styles have weakened consistency, accountability and enforcement. They provide scope for subjective interpretation of law, while leaving some parts of the governance framework unregulated. The different legal styles create inconsistent and inappropriate institutions and hinder the development and understanding of democracy, professionalism, transparency, and accountability.

Implementation of laws remains a problem. This is exacerbated because the social and political role of the law is not fully understood. Frequently, public sector institutions do not hesitate to disregard legal provisions or binding procedures as they see fit. This problem seems to be a matter of legal culture, which needs to gradually evolve through a long-term process.

Constitution

Bosnia and Herzegovina's (BiH) constitutional set-up, which was arranged to end the wars on BiH's territory, deprived local politicians of responsibility and real accountability, as these were assumed by the international community, mainly through the Office of the High Representative (article 5 Annex X of the General Framework Agreement). This set-up is an unsuitable basis for an effective democratic state, as it pre-empts the possibility of creating a sufficiently empowered central state, while enshrining an ethnic and religious-based polity. Furthermore, the current Constitutions have generated an extraordinary and unmanageable collection of legal orders with 14 governments, including the State, the Federation, Republika Srpska (RS) and the cantons (not counting Brčko). The constitutional system distributes veto rights widely amongst political actors and over numerous "veto points" on a multiplicity of so-called "vital national² interests". The system is inimical to rational decision-making and prevents the emergence of a habit of political compromise inherent to any democratic regime. The State has, in reality, almost no power to modify the power sharing arrangements, which are protected by the international community. An assessment of the effectiveness of the functioning of the State cannot be decoupled from an assessment of the functioning of the international community, its capacities, and the checks and balances under which it operates. The international community has tried several times, since 2006, to promote a more workable constitutional set-up but has so far not succeeded. BiH's current constitutional set-up therefore continues to be incompatible with the current requirements for EU membership.

Parliament

The legislative function of the Parliaments is directly affected by the weaknesses of the Constitution and the weak professional policy capacities of both the international community and the governments. The religiously and ethnically based distribution of parliamentary seats, based on 1991 census data (i.e. pre-war and now wildly inaccurate), and recurrent ethnic-based voting by the electorate, not only reduces the Parliaments' public legitimacy, but also its ability to contribute solutions to the actual problems affecting the country: poverty, unemployment, ethnic and religious hatred and a dysfunctional public administration and other institutions.

² Meaning Bosniak, Croat or Serb communities

Government

The system of multiple governments with radically opposed political agendas is aggravated by the weak influence and power of the central institutions of the State. The large reform plan – the implementation by the State, Entities, and the Brčko District of a joint programme to reform their Centres of Government (the “Blueprint Project”) – is seriously delayed.

A Commission on European integration, chaired by the Director of the Directorate of European Integration (DEI), manages European Integration. In 2010 the DEI initiated a fundamental review of the co-ordination mechanisms for managing the EU accession process, with a view to improving performance and addressing present and future requirements. Following a thorough assessment of current co-ordination mechanisms and consultations with relevant state, entity and Brčko District institutions, a draft Decision on a revised co-ordination process has been prepared. The new proposal for a Decision on co-ordination will be submitted to the Council of Ministers for adoption following additional consultations.

Public administration

The disorganisation of public institutions and wasteful administration are two of the main characteristics of BiH’s administrative legal framework and civil service systems. The administrative system is burdensome, expensive and contradictory across the various levels of government. The vested interests of the BiH constituents have resisted changes to the Dayton Peace Agreement (DPA) for longer than initially envisaged, hampering the much-needed progress towards the establishment of a modern and efficient government. Ethnic divides are institutionalised in BiH. They mask political patronage and cronyism in the public administration, which are detrimental to its professionalism. BiH suffers from all of the governance problems of the former Yugoslavia (for example, the lack of delegation), but these issues can only be addressed once the DPA has been reformed. Efforts to reform the public administration in BiH have little or no political support from the domestic political forces and have failed to address the acute problems of the administration.

Public expenditure management developments in BiH over the last year continues to be mainly influenced by a Stand-by Agreement (SBA) with the IMF, requiring BiH to concentrate on maintaining macroeconomic stability through fiscal consolidation. However, a range of austerity measures were delayed before the elections of October 2010. During 2010 and into 2011 the economy is expected to improve but the fragile overall political situation led to delays in the adoption of annual budgets. While the Federation adopted its 2011 budget in March 2011, no budget has been agreed for the State so far, primarily because of differences over the impact of the revenue sharing formula upon the finances of the State.

These delays impact upon budget execution because they prevent effective planning and management of public expenditure. This compounds the still existing problems of weak budget planning and management capacities at all levels and adversely affects the potential benefits of introducing public internal financial control (PIFC).

Regarding PIFC, the most important development has been the launch of the Central Harmonisation Unit Coordination Board. It has met monthly since November 2010 and has reached an agreement on a rotating chairmanship, procedures and an initial work programme. This initial programme focuses on internal audit, rather than financial management and control, but under the present circumstances, this may be an appropriate prioritisation.

External audit has developed strongly at the technical level (with support from the Swedish International Development Agency), but this has had limited impact on the reality of the budget execution. The Supreme Audit Institutions (SAIs) have no constitutional standing and parliaments have only just started using their reports.

Public procurement reform has been on hold for a number of years. Since 2007 all initiatives to modernise the Public Procurement Law have failed in parliament. The regulation of concessions and public-private partnerships (PPPs) remains worrisome; it is fragmented and lacks transparency and openness.

Judiciary

No legal certainty can be guaranteed in a country where there is no supreme judicial instance empowered to unify legal doctrine and impose its legal interpretation on lower courts. The organisation of administrative justice needs to be done countrywide and needs to be established as a clearly designed hierarchy of courts. The current set-up for administrative justice is unfit to guarantee that the various existing administrations will abide by the rule of law. A countrywide unified law on administrative justice is needed and it should endow administrative courts with full jurisdiction and create better instruments to oblige administrative authorities to “refer the file” to the court and to ensure more effective enforcement of administrative court rulings pronounced against public authorities. However, the constitutional basis for such a court is missing. The relevant authorities have not commenced the implementation of the National Judicial Reform Strategy agreed in the framework of the Peace Implementation Council and Council of Europe.

Anti-corruption

Corruption remains a very serious problem and government efforts to combat it have been weak. The complexities of the institutional set-up are not conducive to a reduction of corruption or an efficient anti-corruption policy. On the contrary, the complexity and weaknesses of BiH’s public governance system make it prone to capture by private (or other) interests. The lack of progress in fighting corruption is reflected in the BiH’s consistently low scores in relevant international and domestic surveys. The existence of the Anti Corruption Strategy has not contributed to the advancement of anti-corruption reforms. Into its second year, the Strategy remains for the most part unimplemented, and it has had little influence among politicians and political parties. The dramatic level of corruption in Bosnia and Herzegovina has not been on the decline over the last few years. Reforms, when they are carried out, are still largely motivated by outside pressure. The Agency for the Prevention of Corruption and the Co-ordination of the Fight against Corruption was established by law at the end of 2009. A functioning agency has been one of the conditions for BiH to benefit from visa liberalisation with the EU. Visa liberalisation was granted in November 2010, notwithstanding the fact that the anti-corruption agency was not functioning at the time. Since then, decisions on the appointment of a head and deputy head of agency have not been taken.

Recommendations

The Washington and Dayton Peace Agreements were a diplomatic success and were instrumental in bringing the war in Bosnia and Herzegovina to an end. However, they also created an unmanageable administrative set-up in FBiH and BiH. They also confirmed the dominance of ethnic based political rights over individual political rights, thus undermining the principles of liberal democracy. Reforming the constitutional foundations of FBiH and BiH is key for progress in public administrative reform and the creation of an effective state apparatus. The international community should continue its efforts to facilitate constitutional reforms by building a consensus and supportive climate.

In the meantime, BiH’s authorities should focus on implementing the reforms agreed so far. Some of them, already formally adopted (under pressure from the international community), have not had any impact since BiH’ authorities have failed to implement them.

BiH’s authorities, supported by the international community, should also undertake serious efforts to start implementing the already adopted National Anti-Corruption Strategy. The Agency for the Prevention of Corruption and the Co-ordination of the Fight against Corruption should be staffed and provided with an adequate budget for its functioning and operations.

BiH's authorities should implement legislation and activities aimed at establishing a merit-based civil service system and at improving the transparency, accountability and performance of the administration, especially in areas that have a direct impact on citizens' rights and on the business climate.

CIVIL SERVICE AND ADMINISTRATIVE LAW

Main Developments since the Last Assessment (May 2010)

Developments in the civil service and in the administrative legal framework have generally been rare and uneven across Bosnia and Herzegovina (BiH), with Republika Srpska (RS) progressing more rapidly than BiH (state level), the Federation of BiH (FBiH) and the Brčko District. Most of the progress has been achieved under the pressure or with the assistance of donors, with the associated risks of increased inconsistencies and lower ownership. This has been the case, for instance, of the usage of the (donor-financed) Public Administration Reform (PAR) Fund. Drawing lessons from the limited achievements in the implementation of the Action Plan which benefited support from the PAR Fund in 2009 and 2010, a revised Action Plan for the period 2011 – 2014 was designed. The general approach to the revision of the previous action plan was to reduce drastically its level of ambition. While the Public Administration Reform Co-ordinator's Office (PARCO) has been established to co-ordinate administrative reforms within and across government levels of BiH, its position, capacity and leadership and the lack of acceptance by the government levels (especially RS) seriously undermine its ability to initiate and manage change.

A Standby Agreement (SBA) with the IMF was signed in 2009 to deal with a severe drop in public revenue. The SBA calls for a range of reforms in BiH and requires (among other measures) the adoption of a new Law on Salaries for public sector employees. It also requires budget cuts for the wage bill and budget adjustments. In December 2010, the RS Government amended the Law on Salaries by extending into 2011 the provision to cut by 10% the salaries of non-managerial staff and up to 25% the salaries of senior staff and political appointees. All governments reduced the percentage of recruitment approvals in 2010. However, so far the financial crisis has caused no major lay-offs in BiH administrative structures. In the **civil service** area, marginal positive changes have been made since the last SIGMA assessment. The Federation of BiH remains the most problematic due to the disarray in which the civil service structure has found itself following the FBiH Constitutional Court decision to deprive the Civil Service Agency (CSA) of authority at cantonal and municipal levels. So far, only the West-Herzegovina Canton has formed its own agency; five cantons have enacted laws that allow for continuation of the use of the Federation Civil Service Law, and the CSA therefore continues to extend its services to these cantons. Four cantons are still undecided, and it is unclear as to which legal basis they are using in the management of their civil servants. The fragmentation of the FBiH civil service system among cantons is problematic. It is costly and will undermine the coherence and consistency of civil service management in FBiH. It is likely to create further constraints on mobility and incompatibility across civil service systems. Most important, it has the potential to threaten and further weaken the cohesion of the entire FBiH level of government. The fragmentation of the Civil Service Management System across BiH is weakening the accountability chain and the rule of law.

Two developments are symptomatic of the current backsliding of civil service reform. First, there is considerable pressure to re-politicise the civil service. Ministers, MPs and political parties in general seek to enhance political control over the civil service, for instance by facilitating senior-level appointments, facilitating dismissals or, as a kind of compromise, introducing fixed-term appointments for secretaries and assistant ministers. Fixed-term appointments are not necessarily a problem *per se*, as they also exist in many EU Member States, but such a move is likely to send the wrong signal to both the political class and the civil service (uncertainty and increasing political dependence) in an already unstable setting such as that of BiH. In addition, the weak economy and high unemployment create major incentives for parties to distribute patronage goods, including public jobs, to their supporters. Second, considerable pressure for the fragmentation of the civil service has emerged in BiH. The presence of three levels of government has

already created a degree of differentiation that distinguishes BiH from the other Western Balkan states, in particular due to the lack of a BiH-wide umbrella/framework law on the civil service, which would facilitate co-ordination across levels and establish system-compatibilities (rather than harmonisation, often understood as having identical laws, which is clearly unnecessary, as already pointed out by SIGMA in 2008 and more recently in 2011). The Civil Service management capacities at all levels in BiH remain generally weak.

In the area of **administrative law**, numerous technical laws and by-laws or amendments to existing laws have been adopted at BiH State, FBiH, RS and Brčko District levels since last year's assessment. At the **state level**, the Parliamentary Assembly of Bosnia and Herzegovina adopted the Law on Amendments and Supplements to the Labour Law in the Institutions of Bosnia and Herzegovina (*Official Gazette of Bosnia and Herzegovina*, no. 60/10). The Council of Ministers of BiH adopted the Rulebook on Amendments and Supplements of the Rulebook on Disciplinary Responsibility of Civil Servants in the Institutions of Bosnia and Herzegovina (*Official Gazette of Bosnia and Herzegovina*, no. 94/10). The Civil Service Agency of Bosnia and Herzegovina adopted the Rulebook on Conditions and Method of Publishing Competitions, Internal and External Transfers of Civil Servants in the Institutions of Bosnia and Herzegovina (*Official Gazette of Bosnia and Herzegovina*, no. 96/10). The Government of the **Federation of Bosnia and Herzegovina** and the International Financial Corporation (IFC) have begun implementation of a regulatory reform project at the Federation level. In September 2010, the Federation Government defined the draft Law on Registers [of Births, Marriages and Deaths] in the Federation of Bosnia and Herzegovina. The new provisions being introduced reflect the necessity to conform to new technologies and to the options that they offer in order to improve the quality of services to citizens. The Constitutional Court of the Federation of Bosnia and Herzegovina, at its session held on 20 April 2010, made a decision that declared the provisions of the Federation Civil Service Law related to cantons, municipalities and cities to be unconstitutional (decision published in the *Official Gazette of the Federation of Bosnia and Herzegovina*, no. 34/10). In **Republika Srpska**, the Law on Amendments and Supplements to the Law on General Administrative Procedure was adopted in May 2010 (*Official Gazette of the Republic of Srpska*, no. 50/10). The new law, *inter alia*, provides for delegation of power. It also prescribes the duty of the second-instance decision-making body, in the event of re-deciding a case, to take the decision itself *in merito*. The amendments also introduced electronic communication between the parties, as well as conditions to be met by the official in charge of conducting the administrative procedure and taking the decision. In November 2010, the Government of Republika Srpska launched a project on electronic law-making (e-law-making). The project encompasses the establishment of a database of all laws and regulations in Republika Srpska, to be accessed through the integrated Internet portal. The RS Ministry of Administration and Local Self-Government issued the Instruction on Implementation of the Law on Authentication of Signatures, Handwritings and Copies. In December 2010, the National Assembly of Republika Srpska adopted amendments to the Law on Salaries of those employed Republika Srpska Administrative Organs. These amendments reaffirmed the salary cuts introduced in 2010. In the **Brcko District**, the Assembly of the Brcko District adopted in June 2010 the draft Law on Electronic Documents and the draft Law on Electronic Signature.

State-level authorities decide on administrative cases by applying the 2002 Law on Administrative Procedure (LAP), which is similar to the administrative procedure laws in force in the entities. An LAP was passed in the FBiH in 1998 and in the RS in 2000. Differences between them stem mainly from their respective territorial/political organisation. Indeed, all of these laws are part of a same practice dating back to the Socialist Federal Republic of Yugoslavia (SFRY) Law of 1956, which in turn was based on the *Law on General Administrative Procedure of the Kingdom of Yugoslavia* of 1930, which represented a development of the Austrian Law on Administrative Procedure of 1925. In terms of capacity to apply the LAP, it is to be noted that the practice of administrative decision-making in State institutions is far from sophisticated.

The cantons have produced their own legislation, which often is not aligned with the entity and state legislation. The existence of numerous and different laws and regulations on administrative procedures at state, entity and canton level impinges upon the rights of citizens, legal certainty and, ultimately, on the rule of law. Despite the common roots of law in the various jurisdictions, the international donor

community, through its assistance programmes and its leadership role, has worsened the divergence in the development of legal frameworks. In spite of some modernisation, the Laws on Administrative Procedures in BiH still reflect the authoritarian understanding of public administration of the past, does not provide complete legal protection against administrative decisions, stipulates unnecessarily complicated and lengthy procedures, and goes into regulatory details that would be better dealt with through secondary legislation or internal administrative rules. This contributes to corruption and prevents the emergence of BiH citizenry.

No legal certainty can be guaranteed in a country where there is no supreme judicial instance empowered to unify legal doctrine and impose its legal interpretation on lower courts. The organisation of administrative justice needs to be developed at countrywide and established as a clearly designed hierarchy of courts. The current set-up for administrative justice is unfit to guarantee that the various existing administrations will abide by the rule of law. A countrywide unified law on administrative justice is needed and it should endow administrative courts with full jurisdiction. It should also create better instruments to oblige administrative authorities to “refer the file” to the court and to ensure more effective enforcement of administrative court rulings pronounced against public authorities. However, the constitutional basis for such a court is missing. The relevant authorities have not commenced the implementation of the National Judicial Reform Strategy agreed in the framework of the Peace Implementation Council and Council of Europe.

Main Characteristics

The disorganisation of public institutions and wasteful administration are two of the main characteristics of BiH’s administrative legal framework and civil service systems. Other international organisations have made similar analyses of the situation. The administrative system is burdensome, expensive and contradictory across the various levels of government. The vested interests of the BiH constituents have resisted changes to the Dayton Peace Agreement (DPA) for longer than initially envisaged, hampering the much-needed progress towards the establishment of a modern and efficient government. The few developments since SIGMA’s previous assessment of the civil service and administrative legal framework in BiH confirm that the system is heading in the direction of a continuous struggle to enlarge competencies, at all levels and both horizontally and vertically, thereby creating a difficult legal and political/administrative system. Ethnic divides are exacerbated in BiH. They mask political patronage and cronyism in the public administration, which are detrimental to its professionalism. BiH suffers from all of the governance problems of the former Yugoslavia (for example, the lack of delegation), but these issues can only be addressed once the DPA has been reformed. In the meantime, there is room to work on technical, lower-level improvements.

The fragmentation of the civil service at FBiH level is also closely related to the re-politicisation of the civil service. Fragmentation inevitably weakens the centre, i.e. in this case the FBiH Civil Service Agency. It is likely to create new opportunities for politicisation at the canton level. In 2010, central HRM institutions adopted a uniform HRM information system, which indicated the potential for intra-BiH co-operation. This project was also supported and promoted by the international community. Unfortunately, the HRM Information System project (HRMIS) was struck a triple blow: first, the entity-level civil service agencies refused to start with its implementation; second, at the state level, only a handful of institutions actually began to populate the new database with fresh data; third, the Agency for the Protection of Personal Data (state level) issued a decision forbidding the Civil Service Agency to collect civil servants’ personal data and requesting the erasure of the data that had already been collected. The justification is that the CSA has no legal basis to collect the range of personal data required by the HRM Information System. The CSA is currently working on amending the Civil Service Law to include a provision that will serve as the basis for the data collection process, but the approval of the Agency for the Protection of Personal Data will have to be obtained.

Reform Capacities

Efforts to reform the public administration have received little or no political support from domestic political forces and have failed to address the administration's acute problems. These problems include inadequate human resources, overlapping competencies, lack of co-ordination between and across levels of government, absence of a consensual or co-operative administrative culture, and continuous political interference in the hiring and management of civil servants.

BiH's institutional complexity makes reform almost impossible. A complex and inefficient administrative structure slows down decision-making processes and is responsible for top-heavy public spending. The lack of consensus on the nature of the state contributes to the slow and uneven administrative transformation in BiH. Many of the public governance reforms are donor-driven. In the absence of strengthened co-ordination, foreign input to reforms at various levels might even increase the existing fragmentation and inconsistencies of the administrative systems of BiH.

Problems also result from BiH's current political/administrative structure, which does not allow for arbitration between competing interests. Given the practical absence of generally accepted arbitration mechanisms, decision-making is based on consensus-building at all levels (therefore with multiple veto points), from canton and entity levels to state level. The protection of so-called "Vital National Interests" (established – but not defined – by the Dayton Peace Agreement) allows communities to block decision-making in parliament and in most governments. Several decisions of the Constitutional Court have restricted the scope of such actions in recent years, but the "Vital National Interests" continue to paralyse the decision-making process. Many of the attempted reform policies have been internationally imposed or negotiated under international supervision, while implementation has been left to inadequate BiH institutions and to politicians who opposed the reforms. Most of these reforms would not stand without the persistent pressure of the international community.

In light of the current constitutional limitations, the role of the National PAR Co-ordinator (PARCO) in ensuring progress in this area remains positive and has been crucial for the implementation of any reforms. However, it is to be noted that the role of PARCO is being marginalised by domestic authorities. For instance, PARCO is unfortunately not in a position to co-ordinate in substance the process of drafting and enacting legislation. There have been several recommendations to strengthen the existing monitoring and co-ordination capacities at state level, but such recommendations are likely to be vetoed by the entities.

Recommendations

1. Secure a country-wide unified regime of administrative procedures that would contribute to the creation of BiH's internal market. Create an administrative court with geographical competencies over the whole of BiH.
2. Promote merit based civil services in all entities without necessarily harmonising the different civil service laws.
3. Put in place a system to restrain further fragmentation of BiH's politico-administrative system.

INTEGRITY

Main Developments since the Last Assessment (May 2010)

In 2009 Bosnia and Herzegovina (BiH) adopted the National Anti-Corruption Strategy 2009-2014 (ACS) and a relevant Action Plan (AP). By early 2011, very little progress had been made in implementing the ACS. A survey conducted by the BiH chapter of Transparency International found that the specific measures and deadlines of the ACS were insufficiently known to the institutions that were supposed to implement them, and that only a few measures were being implemented (mainly those that overlapped with the Public Sector Reform Strategy, coordinated by PARCO). This situation was primarily attributed to a lack of overall co-ordination caused by the fact that the Anti-Corruption Agency was not yet operational and by the lack of resources to support the measures.

The Agency for the Prevention of Corruption and the Co-ordination of the Fight against Corruption was established by law at the end of 2009, and an acting head of the agency was appointed, whose mandate has been extended several times. An ad-hoc parliamentary commission drew up a shortlist of candidates, who participated in an open competition for the post of agency head. A functioning agency has been one of the conditions for BiH to benefit from visa liberalisation with the EU. Visa liberalisation was granted in November 2010, notwithstanding the fact that the anti-corruption agency was not functioning at the time. Since then, decisions regarding the appointment of a head and of a deputy head of agency have not been taken. The absence of formation of a government following the October 2010 general elections has since then been used as an excuse for not making these appointments, postponing the actual implementation of the agency. At the time of writing, these appointments have not yet been made. Beyond these appointments, concerns have been raised in the media and among civil society groups that the agency could remain seriously under-resourced, resulting in an insufficient capacity to implement the ACS, and could not have the power to implement its mandate vigorously as a result of the lack of a general political will to address corruption in the country.

A new Law on Political Party Financing was adopted by parliament on 24 June 2010. The law has raised the financial threshold for donations by legal entities from 8 times to 15 times the average annual salary after tax. Political parties are also now obliged to keep evidence concerning the sources of their income and to issue receipts to donors (physical or legal entities). A 2010 report by Transparency International (TI) BiH highlighted numerous violations of the previous law, based on a review of the political parties' financial reports to the Central Election Committee. The reports also provided sufficient evidence for TI to conclude that these violations remained largely unpunished.

With regard to legislation on the freedom of access to information, there has been considerable resistance to deal with requests concerning privatisation, public procurement, and development banks. Furthermore, the legislation has still not been harmonised between entity and state levels, leading to inconsistent application of the legislation.

Main Characteristics

The Agency for the Prevention of Corruption and the Co-ordination of the Fight against Corruption was established by law at the end of 2009, but as a result of the lack of general political will to address corruption in the country, it has not been made operational.

The Anti-Corruption Strategy (2009 – 2014) focuses on capacity-building of the new Agency; preventive measures of a generic nature, such as simplified and stricter administrative rules and procedures and greater transparency and accountability; education and training; and law enforcement, co-ordination and international co-operation. The ACS is comprehensive and, if implemented, would contribute reducing the level of Corruption in BiH.

The lack of progress in fighting corruption is reflected in the consistently low scores of BiH in the relevant international and domestic surveys. BiH has not substantially improved its rating in Transparency International's Corruption Perception Index since 2007. The annual Nations in Transit report of the think-tank Freedom House broadly echoes these findings: its 2010 report rates BiH as 4.50 for the criterion of corruption (on a descending scale, where 7 is the worst and 1 the best possible rating); this rating is broadly similar to the ratings of previous years. The local chapter of Transparency International in BiH has identified administrative corruption as being the most widespread at local level, as well as in the health and education sectors; political corruption has been highlighted by the organisation as the main impediment to overall political reform in BiH.

Corruption in the judiciary remains a major challenge in BiH. The level of corruption in the judiciary is a serious constraint for doing business in the country. Citizens lack confidence in the judicial system that they perceive as one of the country's most corrupt institutions. The judiciary is struggling to gain its independence from the government. Respect for the rule of law tends to be selective and independent judges have reportedly faced various forms of threats and intimidation. Despite the initiation of reforms, courts remain slow and inefficient, due to weak judicial structures and professional standards. Excessive delays in the criminal justice system and overwhelming backlogs of cases continue to hamper the effective delivery of justice.

There is no functioning law on conflict of interest. This might be an indication of the lack of political interest to deal with the problem. At the end of 2009, a new version of the Law on Conflict of Interest was submitted to parliament. The new draft law was widely criticised by various international players, who feared a watering-down of the existing law by a loosening of the provisions on the compatibility of public and private offices as a consequence of a number of high-profile rulings by the Central Election Commission that oversees, *inter alia*, the implementation of the law. A working group at ministerial level was formed to reconcile various versions of the new draft law, but this group did not meet in 2010, and there have been no further developments with regard to its potential adoption.

The Central Election Commission has continued to publicly file income and asset declarations of elected officials, and it has issued fines to several individuals who had failed to submit their asset declarations on time. However, the media has reported on a number of cases of elected officials who significantly under-declared their assets.

In addition to Transparency International (TI), a number of other civil society organisations are concerned with addressing corruption. TI recently convened a meeting of relevant organisations to discuss options for civil society action to apply pressure for the implementation of the ACS. The Centre for Investigative Reporting is one of the key players producing publications on corruption.

Reform Capacities

The existence of the ACS has not contributed to the advancement of anti-corruption reforms in BiH. Into its second year, the Strategy remains for the most part unimplemented, and it has had little influence among politicians and political parties. The dramatic level of corruption in Bosnia and Herzegovina has not been on the decline over the last few years. Reforms, when they are carried out, are still largely motivated by outside pressure.

The complexities of the institutional set-up derived from the Dayton Agreement are not conducive to reducing corruption or to developing efficient anti-corruption policy. On the contrary, the complexity and weaknesses of the public governance system in BiH make it prone to capture by private (or other) interests.

Recommendations

Unless there is political will to fight corruption, no technocratic action will be effective fighting it. However, the following measures can be explored in the short term:

1. As a priority, the international community should support the governments of Bosnia and Herzegovina in strengthening their integrity frameworks. This means promoting a systemic and comprehensive approach to integrity management within government. It may combine the integrity management systems (the instruments, processes and actors within public sector organisations to stimulate and enforce integrity and prevent corruption) and the integrity context (or supporting environment) that will impact on the integrity of members of public sector organisations.
2. Since the decision to create the Agency for the Prevention of Corruption and the Co-ordination of the Fight against Corruption has been taken, the Government should staff it and provide it with an adequate budget for its functioning and operations.

The laws on Political Party Financing should be implemented. A law on conflict of interest that meets the relevant international standards should be adopted and implemented. Financial accounts of political parties could be checked and audited by independent, commercial, and preferably foreign auditing companies

PUBLIC EXPENDITURE MANAGEMENT AND CONTROL¹

Main Developments since the Last Assessment (May 2010)

In Bosnia and Herzegovina (BiH), the global financial crisis and subsequent recession resulted in the budget deficit widening to 5.7% of GDP in 2009 and remaining large in 2010, at an estimated 4.5%. In mid-2009, BiH signed a three-year Stand-by-Agreement (SBA) with the IMF, to help finance the budget and current-account deficits. Under the Arrangement, the consolidated budget deficit was limited to 4.5% of GDP in 2010 and 3% of GDP in 2011. The specific objectives of the SBA are to: reduce the structural fiscal balance to limit the government's financing needs and bring public finances on a sustainable medium-term path; re-establish public wage restraint; support adequate liquidity and capitalisation of banks; secure sufficient external financing; and improve confidence.

To achieve these targets, some cuts in public-sector pay and in war veterans' benefits have already been made in 2009 and 2010. However, there has been some delay in achieving some of the targets, such as the approval of the law to forbid the passing of unfunded legislation by the Federation (fiscal responsibility law). Some IMF disbursements have been held up because of these delays.

Public debt amounted to approximately 39% of GDP in 2010 (IMF estimate).

Actual changes during the past year in the **public expenditure management (PEM)** arrangements have been limited. Overall, the situation has remained fragile and at the end of March 2011, a budget had still not been agreed for 2011 for the BiH State, the Federation budget was only agreed in March. As a result of this delay, the State now has to rely on temporary financing until June, when temporary financing will have to be extended if necessary. Republika Srpska adopted its budget for 2011 on time.

The difficulties with regard to budget-setting have arisen for two reasons. First of all, at State level, no government has been formed so far since the October 2010 elections. In the Federation, a government was only formed in March. Secondly, and this factor potentially affects the state and entity governments, no agreement has been reached on the arrangements for the financing of the state. If the present revenue-sharing formula is maintained, the state will face a significant deficit because a carry-forward of surplus revenues from previous years is no longer available. If the revenue-sharing formula is revised, the currently agreed budget of Republika Srpska will be disturbed and the Federation will also be affected, as both will lose funds, to the benefit of the state. The Fiscal Council, created in 2008 and consisting of the three prime ministers and ministers of finance, has been unable to resolve this deadlock.

The governments of the state and of both entities have now adopted a revised chart of accounts and new fiscal reporting requirements that are consistent with the requirements of GFS 2001. The Federation Treasury has added a new cash-flow control module (in accordance with a World Bank conditionality).

Programme budgeting is continuing to develop in the State and the entities, with support being provided by the European Union (EU) now that the technical assistance project funded by the UK Department for International Development (DFID) has come to an end.

¹ This report does not assess developments in Brčko District

In BiH State, the Budget Directorate has been strengthened by the appointment of three additional staff.

With regard to **public internal financial control (PIFC)**, an element of real progress has been the formal appointment of the head of the State's Central Harmonisation Unit (CHU) in July 2010 and of the Federation's in March 2011 (the head of the RS CHU having already been appointed). All CHUs have two units: one for Internal Audit (IA) and one for financial management and control (FMC). In November 2011 the Co-ordination Board of the three Central Harmonisation Units (CHUs) was established. The Co-ordination Board, whose members are the heads of the CHUs, has met monthly since its establishment at the end of November 2010. An agreement has been reached concerning a rotational presidency (starting with the State CHU), the organisational procedures that the Board will adopt as well as the programme of activities for the first part of 2011, which will focus on internal audit. Work on developing financial management and control (FMC) by the Board has been deferred until later on, due to a shortage of resources within the CHUs. However, some discussions on the necessary legal basis for FMC have started within the State. A technical assistance project to support the CHUs started in 2010.

In the area of **external audit**, the three supreme audit institutions (SAIs) have continued to perform well, but they still have limited impact on public financial management. In 2010 the external audit Co-ordination Board revised guidelines for financial and performance audit, issued guidelines for quality control, and adopted the International Standards of Supreme Audit Institutions (ISSAIs) as a framework for its professional work. In 2010, the audit offices of Republika Srpska, the State, and the Federation issued respectively 53, 60 and 68 financial audit reports. All three audit offices started performance audits over the last 12 months (two in the State and the Federation and 3 in Republika Srpska), which are ongoing with the support of the Swedish National Audit Office.

All audit offices have increased their staff: from 57 to 61 in the Federation, from 53 to 59 staff in Republika Srpska and from 38 to 48 staff in the State. Due to the elections in 2010, the parliaments have not fully discussed the SAI annual reports; in the State, the SAI's annual reports for 2009 and 2010 might be discussed simultaneously in 2011.

Main Characteristics

BiH currently relies on IMF funding to finance its deficit, and the conditions of IMF funding require a reduction in current expenditure, especially in labour costs and in pensions and other social transfer costs, and a switch to investment expenditure. The economy is improving, which should lead to an overall increase in revenue. However, the outlook remains uncertain, especially as the State has not yet been able to agree a 2011 budget.

The main conditions of the SBA are currently being largely met although it is unclear how far the reviews of the privilege pensions and the audit of war veterans payments is producing the savings anticipated. The present dispute between the State and the entities over the revenue sharing formula has created budgetary uncertainty which in itself will add to the difficulties of achieving the fiscal consolidation objectives of the SBA. One of the main characteristics is the lack of co-ordination between the state and entity governments, which affects in particular the public expenditure systems. While the Indirect Tax Authority (mainly responsible for the enforcement of legal provisions and policy on indirect taxation, as well as for the collection and allocation of indirect tax revenues) has been operating successfully since 2005, the Fiscal Council (mainly responsible for co-ordinating fiscal policy), in operation since 2008, appears overall to be less successful, with views about its success reflecting each government's perceptions. More recently, the CHU Co-ordination Board began its operations and initial indications are promising, but in a number of areas co-ordination is still lacking.

The State and both entities – the Federation and Republika Srpska – all have in place basic budgetary legislation regulating financial management issues. The Law on Financing the Institutions of Bosnia and

Herzegovina (2004) regulates the preparation, enactment, execution, accounting, reporting and supervision of the budget, the Treasury Single Account, and the investment of public monies of BiH State. In Republika Srpska, the Law on the Budget System (2003) lays down the regulations for the preparation, planning, development, adoption and execution of the budget, as well as for budget accounting, control and audit. The Law on Budgets (2006) regulates the planning, development, enactment and execution as well as debt management, accounting, reporting, supervision and revision of the budget in the Federation of Bosnia and Herzegovina. In both entities the laws provide regulations for all levels of the government, including municipalities, as well as for extra-budgetary funds.

The legal framework regulating public expenditure management in its substance differs substantially between the state and both entities. Among other issues, each of the three governments has had a different budget calendar and has used different budget preparation, accounting and reporting methodologies, with different charts of accounts. These differences have resulted in unreliable financial statistics.

In terms of procedures for the budget preparation, the Fiscal Council adopts a policy document setting out the fiscal framework for the next three years, covering three main elements, namely: fiscal objectives, a macroeconomic analysis and policy concerning indirect taxes, and upper limits of debt. The resulting document is then signed as an agreement between the three governments. Based on this framework, the annual budget and a three-year Medium-Term Expenditure Framework (MTEF) is to be prepared for the state and entities.

During 2010 the Fiscal Council has had to address the financial crisis and respond to the conditions laid down in the IMF Standby Agreement. The extent to which it has acted as a co-ordinating body and as a decision-making body in these circumstances is unclear. It appears so far to have been unable to make decisions to resolve the crisis caused by the disagreement over the funding of the state.

The budgets of the State and the entities seem to be reasonably comprehensive and the central governments' definitions of 'general government' includes budgetary, extra budgetary and social security funds. Donor funded expenditure, whether from loan or grant appears not to be included.

A weakness of public expenditure management in Bosnia and Herzegovina is the lack of effective medium-term financial planning. Work in this area is being undertaken in each Ministry of Finance, but at present there is no effective linkage between such plans and the annual budgets. Another weakness is the lack of experienced staff capacity. However, the possibility of further staff increases will inevitably be limited by the current public expenditure restrictions.

A further problem is that even though Bosnia and Herzegovina has had to manage a serious financial crisis and pressure from the IMF to develop more realistic expenditure policies, political pressures for additional public expenditure appear to remain. In Republika Srpska, for example, educational spending and numbers of staff have increased in order to reduce class sizes in schools from between 30 and 35 to 25. In BiH State, proposals have been approved by parliament (but have been opposed by the Ministry of Finance and the Treasury and are now being challenged in the Constitutional Court) to pay pensions to members of the armed forces who are demobilised, whatever their age (a form of privileged pension arrangement that was criticised by the IMF). In the Federation, pressure on some cantons to prepare more realistic and less expansionary budgets still appears to be "work in progress". The analysis of proposed investment projects for the purpose of identifying ongoing current costs and establishing overall costs and benefits is limited. While some work has been undertaken to determine the long-term viability of some funds (e.g. in Republika Srpska), overall strategic financial planning is lacking.

While the pressures to respond to social needs is understandable, strengthened governmental processes are required to balance these social needs against other needs, such as infrastructure investment and reduced demands on taxpayers.

Each Treasury is pursuing its own independent technical development strategy. None appears to be willing to co-operate with the other Treasuries in this development. Each has absorbed quite readily the reforms required by the single chart of accounts and the new arrangements for financial reporting. Again, as the demands for expansion of the Treasury systems increase with the establishment of new public sector organisations, these changes are also readily accommodated. The Treasury systems are the principal instruments of internal financial control and from that point of view they are operating efficiently. However, co-operation between the systems ought to lead to more cost-effective development, although agreement on priorities would be required. Each Treasury system records commitments to a certain degree (which varies between the different governments), but an overall stronger control over commitments would serve to strengthen public expenditure management by ensuring that no commitment was entered into unless funds were actually forecast to be available at the time payment was due to be made.

Public internal financial control (PIFC) is still in a very early stage of development. After the adoption of harmonised internal audit laws by the state and entity governments in 2008, harmonised PIFC policy papers were adopted in 2009 by BiH State and in 2010 by the entities, and they are now being implemented. CHUs have been established in BiH State and in the entities, although the CHUs in BiH State and in the Federation are still significantly understaffed. However, all heads of CHUs have an appropriate status, and now that the CHU Co-ordination Board has been established and is operational, further harmonised development should be possible.

Financial management and control (FMC) at present relies on the existing budget laws. The Coordination Board intends to address FMC only when it has completed its present work on internal audit. However, the State CHU has started consultations on the extent to which legislation concerning FMC should be dealt with in primary legislation and on the FMC issues to be regulated by secondary legislation. Overall, the legal basis for internal control is imprecise. The laws include the requirement to establish internal control as well as internal audit. These requirements are generic, however, and have not been further developed, and the texts do not clearly distinguish between the functions of control, audit and inspection. In other countries, starting with internal audit and addressing FMC reform afterwards, would be inappropriate. Internal audit cannot be effective without strong financial management and control arrangements, nor can it play an advisory role to management. Financial management and control also requires a stable budgetary process coupled with longer term financial planning, as well as a management process that allows for the delegation of budgets and responsibilities. These processes have to be accompanied by appropriate accountability arrangements. Financial management permeates the whole of the budget execution process. This operational environment does not exist in BiH. In these circumstances, the focus ought to be on technical developments and, since internal audit can be defined much more clearly than FMC, starting with internal audit may be appropriate. However, in doing this, the limitations of this approach must be clearly recognised, and internal audit will never become effective without an appropriate structure of financial management and control.

Internal audit throughout BiH is also still in a very early stage of development. The internal audit laws are broadly in line with international requirements, but their implementation is slow. BiH State has approximately six internal audit units, with a total 10 staff; in the Federation there are about 10 internal audit units with 15 staff (in addition, a limited number of units are in cantons and municipalities); and Republika Srpska has 18 units (including in municipalities), with 27 staff. These small numbers, besides any judgment on technical competence, demonstrate how embryonic the development of internal audit is in BiH. However, the fact that the newly established CHUs in the State and the entities are now taking over responsibility for the further development of internal audit, harmonised through the CHU Coordination Board, suggests that despite these small numbers, a platform for internal audit is being established. As the economy improves, further development can take place on the basis of this platform. Internal auditors currently receive training from the technical assistance project that started in 2010.

A key problem in the introduction of a modern PIFC system lays in the current arrangements for the management of public expenditure, in particular the lack of professionalisation of public service management, and the lack of distribution of responsibilities and delegation of authorities within public organisations. Greater professionalisation and the devolution of authority and responsibility, coupled with the development of accountability arrangements, is most likely to result in a more economic, effective and efficient use of public funds. This is a concept that does not yet exist in BiH. Such reforms need to underpin the development of PIFC, and would therefore have to be accompanied by wider reforms in the civil service, including the increased separation of political and managerial responsibilities.

The preparation for decentralised management of EU funds is in an embryonic stage. So far, only the key functions have been appointed in BiH: the National IPA Co-ordinator (NIPAC), the Competent Authorising Officer (CAO), and the National Authorising Officer (NAO). No decision has been taken so far with regard to setting up the Audit Authority (AA), and the institutional position of the AA in the national structure is still under discussion. So far it has not been possible for BiH State and the entities to reach an agreement concerning a government decision on the establishment of functions and a structure for a decentralised implementation system (DIS). Further EU support is now on hold pending concrete decisions on this by BiH. However, more awareness-raising at practical and operational level of the potential possibilities for applying DIS in the specific set-up of BiH may be needed to facilitate this decision making.

External audit in Bosnia and Herzegovina rests on a sound legal basis, but it is still not anchored in the respective constitutions. The work of the Co-ordination Board of Audit Institutions has continued to have a positive impact on the three SAIs and on the development and implementation of common approaches. All three SAIs have acquired reasonable professionalism with regard to financial audits and have also started to prudently develop their capacity for performance audit.

Following the establishment of committees for audit in all three parliaments, which are specifically dedicated to the examination and follow-up of the SAIs' audit reports, there had been an improvement in the use of audit reports by the parliaments, but this progress came to a standstill in 2010 due to the elections. However, recognition of the roles of the SAIs in the respective parliaments has improved. The executive has made, and is still making, attempts to exert influence over the SAIs, in particular with regard to their financial independence. The independence of the SAIs in BiH is thus still fragile in practice, and constant attention from both the SAIs' management and the parliaments is required in order to maintain their institutional and financial independence.

Reform Capacities

The capacity for **PEM** reform depends on the overall economic situation and the ability of the State and entities to form governments capable of carrying through the expenditure changes required under the agreement with the IMF.

The overall key to reform lies in co-operation between the governments of BiH State and the two entities. The Fiscal Council has so far been unable to generate an agreement on the 2011 revenue settlement for the State. Unless the final settlement means that there will be no change in the revenue sharing formula, then any settlement will have an impact on the agreed budgets of the Federation and Republika Srpska. In these circumstances, improving the quality of public expenditure through the implementation of **PIFC** reforms is problematic. Only limited technical reforms can be undertaken that do not have an impact on the overall relationships between or the funding arrangements of BiH State and the entities.

Furthermore, some substantive reforms, such as the development of programme budgeting, are unlikely to be effective without other reforms to management structures and the reorganisation of political/managerial relationships. These reforms would also be needed before significant improvements can be made in the area of public internal financial control. Again, the development of effective medium-

term financial strategies, which would greatly improve the management of public expenditure in BiH State and in the entities and at individual service levels, depends very much on the effectiveness of the Fiscal Council. In turn, the effectiveness of the Fiscal Council depends on the political relationships that can be developed between BiH State and the entities.

The **external audit** institutions are in a privileged position compared to the rest of the public administration, the ministries of finance in particular. The SAIs have significant in-house capacity and commitment to continuous improvement and change. Their knowledge and experience should also be used for the further development of PIFC.

Recommendations

Until overarching relationships between BiH State and the entities become more stable and there is a willingness to implement managerial reforms, the focus of reform should be limited to technical reforms. In some areas, such as internal audit and FMC, expectations of the benefits of reform should be limited to technical improvements, because without improved management arrangements and a stable budgetary process, the operational benefits will not be achieved. Therefore focus of reform at this stage and given the operational circumstances in BiH, if it is to be effective, should be on technical reforms.

Public expenditure management

The treasuries should improve their systems by introducing more effective controls of commitments in BiH State and in both entities.

In the area of budgetary development, the focus of reform in all three ministries of finance - independently of the current financial crisis - should be on improving analytical capacity, the elaboration of an MTEF and its linkage with annual budgets, and the strengthening of the status of the ministries of finance to enable them to more readily resist pressure for increases in social expenditures.

The work to develop strategic financial planning should be extended to cover all funds and to ensure that the recurrent costs of investment projects are fully recognised.

Developments aimed at increasing the capacity to analyse the costs of proposed legislation should continue.

Public Internal Financial Control

- With the newly established CHU Co-ordination Board taking responsibility for the PIFC reforms, a reorientation of the present technical assistance project should be considered in order to focus it as a support to the Board rather than to individual CHUs, while nevertheless recognising that certain CHUs may require specific assistance.
- FMC legislation should be developed and, while resources are limited, such legislation should be set as the next priority.
- Within management structures, the understanding of FMC needs to be increased, while recognising that, until more radical reforms to management arrangements are made, other developments, such as effective risk management, will have to be deferred.
- The CHUs should aim to increase the understanding of both FMC and internal audit among the executive level of administrative authorities, such as ministers, directors of agencies, heads of departments and units in all public organisations.

- Internal audit technical capacity should be enhanced and the establishment of internal audit units extended as economic circumstances allow. A certification scheme for internal auditors should be elaborated.

External audit

With all three development strategies ending in 2012, taking stock by means of a peer review and defining the next steps for further development would be helpful, especially in enhancing the contribution that the SAIs can make to improve the quality of management of public funds in BiH.

- Since according to the laws on the three SAIs the initiative for such a “professional evaluation”, financed by the respective budgets, is to originate from the three parliaments, the SAIs should proactively encourage the newly established parliamentary committees for audit to request that such an evaluation be undertaken.
- In the event that the parliaments do not show any interest in this regard, the SAIs could ask for external support to finance an independent external evaluation.

PUBLIC PROCUREMENT

Main Developments since the Last Assessment (May 2010)

No significant progress has been made in the area of public procurement in Bosnia and Herzegovina since the last assessment.

There has been no major change in the legislative framework for awarding public contracts. As a result of the political deadlock, all of the initiatives undertaken in recent years to modernise the Public Procurement Law (PPL) have failed to be accepted by parliament. In 2010 only one small amendment to the PPL was adopted (Official Gazette BiH, no. 60/10 of 26 July 2010), regulating the validity of the final decisions of the Procurement Review Body – PRB (art. 52 (6) of the PPL). No changes have been made to the secondary legislation. Currently, the Public Procurement Agency (PPA) is finalising a new draft PPL, aimed at closer alignment with the EC Public Procurement Directives. This work started in the autumn of 2010, and the draft is expected to be delivered to the government for approval in April-May 2011 and submitted to parliament during the summer of 2011 (the draft was made available for public consultation in December 2010). The perspectives for its adoption nevertheless remain unclear.

There has been no significant progress in the area of concessions and public-private partnerships (PPPs). The system remains highly fragmented, with separate regulations at the state, entity and canton levels. All of these regulations significantly deviate from EU standards in terms of transparency and access to the market.

On 28 August 2010, the Government of Bosnia and Herzegovina (BiH) adopted a “Strategy for Development of the BiH Public Procurement System in 2010-2015”, but its implementation has, at the time of writing (April 2011), already been significantly delayed. The delay stems at least partially from the general political deadlock in the country, following the parliamentary elections of October 2010.

Currently no technical assistance is provided to BiH’s public procurement institutions (except for the support provided by Sigma).

Main Characteristics

The Public Procurement Law adopted in 2004 generally complies with the main principles of the EU public procurement system (with the exception of domestic preferences), although several discrepancies remain (resulting mainly from the fact that the PPL was modelled on the previous EC Public Procurement Directives that were in force prior to 2004).

The most significant differences with EU public procurement law include:

- Existence of mandatory domestic preferences for local companies offering locally-produced goods and using a local workforce (10% price preference), resulting in discrimination against foreign companies; the decision of the BiH Council of Ministers (adopted on 26 February 2009) extends the duration of domestic preferences until the end of 2014, except for companies from CEFTA countries, which have enjoyed preferential treatment since May 2010;

- Lack of the new procurement techniques and instruments that were introduced in the EU in 2004 (framework agreements, competitive dialogue, electronic auction, social and environmental considerations);
- Slightly different scope of application (private utilities operating on the basis of special or exclusive rights are not included, whereas all public undertakings are included, regardless of the sector in which they are dealing, including state-owned companies operating on a commercial basis in a competitive market);
- Lack of a more flexible system for the utilities sector, as allowed by EC Directive 2004/17;
- Differences in procurement award procedures (e.g. the restricted procedure, accelerated procedures).

The bureaucratic nature of the PPL and its formalistic and simplistic implementation (for instance, unnecessarily extensive and detailed requirements relating to the qualification of suppliers and the frequent rejection of tenders for formalistic reasons, without an analysis of the content) adds to the cost of participation in public tenders (for economic operators) and therefore reduces competition. Non-harmonised regulations at the entity and canton levels and the lack of mutual recognition create additional problems. For example, a construction licence issued in one entity is not accepted in another. In practically all procedures, the criterion of the lowest price is used. The absence of the most economically advantageous criterion could undermine the effectiveness and economy of public procurement by neglecting quality and long-term costs.

The cost (for contracting authorities) of publication of contract notices in the *Official Gazette* remains disproportionately high (200 EUR, regardless of the value of the contract). Some e-procurement tools have been introduced (electronic submission of procurement reports) or are being developed (electronic publication of procurement notices). Still, publication in the paper-based *Official Gazette* remains the main “official” method of publication, and there are no incentives to encourage the wider use of the electronic system.

The existing legal framework for concessions is characterised by fragmentation. The award of concessions by competent authorities is regulated by concessions laws and accompanying laws and decrees in force simultaneously at state, entity and cantonal levels (14 laws altogether). All the laws diverge substantially from EU requirements, in particular with regard to fundamental principles of the EC Treaty. The system dramatically lacks transparency and openness. There is a tendency to award contracts even for big infrastructural projects by using an “unsolicited proposal method” (single-source contracting). The administrative set-up for regulating and managing concessions appears to be extremely complex. Relatively large institutions (Concessions Commissions) are replicated at each level of government – state, regional (entities), and local (cantons).

The central public procurement institutions – the Public Procurement Agency (PPA) and the Procurement Review Body (PRB) – are not sufficiently proactive in disseminating information on the public procurement system and in providing contracting authorities and economic operators with practical assistance. The PPA is currently participating in a large-scale IPA technical assistance project supporting public procurement training in the region. The project will include in-depth training of trainers and the publication of a comprehensive BiH Public Procurement Manual.

The administrative capacity of contracting authorities and the professional ability of procurement officers to properly implement public procurement procedures remain unsatisfactory.

BiH’s business community perceives the practice of public procurement as frequently unprofessional and prone to corruption and political pressure. Apparently there is no political will in BiH to undertake serious

efforts to curb corruption – for example, the establishment of the Anti-Corruption Agency in 2010 had been delayed by several months.

The public procurement review system remains a key concern. It is strongly criticised by both contracting authorities and economic operators for being overly bureaucratic, time-consuming and costly. The quality of PRB decisions is often weak. In the opinion of business organisations, the decisions of the PRB are often too superficial, overlooking the real irregularities and focusing instead on irrelevant formal considerations, which are sometimes unclear and inconclusive. There are also several examples of inconsistent decisions (contradictory rulings in identical or similar situations). Only in December 2010 (five years after its establishment) did the PRB start to publish its decisions online. However, the publication of .pdf documents can be seen as a first step towards transparency. As a second step, there is still a need for a more sophisticated database of decisions, including all past decisions and with browsing and search facilities to allow for the search of individual legal issues. Such a database would also be helpful to PRB members as a means of avoiding inconsistent decisions. The effects of the non-publication of PRB decisions prior to 2011 persist. The trust of the procurement community in the PRB had already been seriously undermined.

Reform Capacity

Although Bosnia and Herzegovina's public procurement system was developing in the right direction in 2004-2006, when the first Public Procurement Law was adopted and its implementation started, obvious signs of weakness and inertia remain. No reform of the public procurement system has been successfully implemented since 2005. Since all of the factors that, in the past, led to the rejection of two previous draft PPLs by parliament (2008-2009) remain in force, it is not certain whether the current attempts to improve the legal framework will be successful. The main reasons for this failure may be found in BiH's political deadlock and in the apparent lack of genuine political commitment to improve the quality of public procurement operations.

The problem has been exacerbated by a deep and permanent conflict between the two main institutions in the sector: the PPA and the PRB. The situation makes any co-operation between those two bodies very difficult. In addition, the PRB has been paralysed by a prolonged internal conflict between the chairman and all of the other members. However, some signs of improvement have recently become visible, both in terms of co-operation between the PPA and PRB and of the internal situation within the PRB.

Recommendations

- Facilitate the adoption of a new Public Procurement Law prepared by the PPA by building a consensus and creating a supportive climate.
- Prepare and adopt new legislation governing the award of concessions and PPP contracts in line with EU standards.
- While continuing to work on a new law, try to simplify procedures and lower the costs of organising (for contracting authorities) and participating in (for economic operators) public tenders; for example:
 - Replace the publication of notices in the *Official Gazette* with electronic publication on the PPA's portal;
 - Introduce a new, simplified system of qualification of suppliers.

- Focus training activities on more efficient procurement tools and techniques (framework agreements, most economically advantageous criteria for contract award);
- Improve the monitoring activities of the PPA;
- Improve the quality and increase the transparency of the work of the PRB;
- Improve the co-ordination between the central public procurement institutions (PPA and PRB).

The recent years have been lost for improvement of the public procurement system in BiH. Most of the activity and energy of the PPA has been focused on futile attempts to pass new legislation. However, most of the above-mentioned recommendations could also be implemented within the existing legislative framework – possibly with a necessity for some minor legislative adjustments, but without adopting an entirely new PPL.

PROCUREMENT/CONCESSIONS STATISTICS for 2010

A. Number of contracting entities		
Central government		72
Regional and local authorities		1100
Other (bodies governed by public law)		565
Utilities		18
Total number of contracting entities		1755
B1. Awarded public contracts/Contracting entities	Total (Euro)	Total number
(Chapter II and III of the PPL)		
BOSNA I HERCEGOVINA	44,222,211	11166
FEDERACIJA BOSNE I HERCEGOVINE	896,314,094	51426
REPUBLIKA SRPSKA	551,909,224	27599
BRČKO DISTRIKT	19,330,345	5758
Total public contracts awarded	1,511,775,874	95949
B2. Awarded concessions/Contracting entities		
Central government	-	-
Regional and local authorities	-	-
Other (bodies governed by public law)	-	-
Utilities	-	-
Total concessions awarded	-	-
C1. Awarded public contracts (Chapter II of the PPL)		
Works	404,711,306	2379
Services	161,928,141	4851
Goods	697,842,455	10270
Mixed contracts	-	-
Total public contracts awarded (Chapter II, PPL)	1,264,481,902	17500

C2. Awarded concessions above the EU thresholds		
Works	-	-
Services	-	-
Other	-	-
Total concessions above the EU thresholds		
D. Procurement methods used (Chapter II of the PPL)		
Open procedure	583,627,077	13795
Restricted procedure	20,872,207	170
Negotiated procedure with prior publication of a notice	3,437,732	46
Negotiated procedure without prior publication of a notice	656,544,886	3489
Other procedures (competitive dialogue, etc.)	-	-
D1. Low-value contracts (Chapter III of the PPL)	247,293,972	-
E. Participation rate (average number of submitted tenders)		
Works	-	3,24
Services	-	2,47
Goods	-	2,75
F. Review procedures		
Number of complaints received	N/a	1831
Number of rulings issued	N/a	1794
Number of appeals against rulings of the review body to the court	N/a	115
Number of decisions with interim measures	N/a	0

F. List of 10 largest procuring entities [name, main activity, (estimated) annual procurement budget]:

1.
2.
3.
4.
5.
6.
7.
8.
9.
10.

G. List of 10 largest public contracts/concessions awarded and/or advertised in 2010 [subject of the contract, name of the contracting authority and contractor (if selected), (estimated) value, time of execution]:

	Entity	Contracting authority	Contract type	Procedure	Supplier	Contract value
1	RS	Javno preduzeće "Putevi Republike Srpske"	Works	Negotiated	Niskogradnja	205,785,040
2	FBIH	Javno preduzeće Elektroprivreda Bosne i Hercegovine d.d. – Sarajevo	Supplies	Negotiated	Rudnici uglja Kreka	54,670,061
3	FbiH	Javno preduzeće Elektroprivreda HZ HB Mostar	Supplies	Open	Energy Finac Team	50,638,660
4	FBiH	Federalna direkcija za civilnu avijaciju	Supplies	Negotiated	Comsoft GmbH	46,263,735
5	FBiH	Javno preduzeće Elektroprivreda Bosne i Hercegovine d.d. - Sarajevo	Supplies	Negotiated	Rudnici Mrkog Uglja Banovići	33,119,364
6	FBiH	Javno preduzeće Elektroprivreda Bosne i Hercegovine d.d. - Sarajevo	Supplies	Negotiated	Rudnik mrkog uglja Kakanj	31,157,048
7	FBiH	Javno preduzeće Elektroprivreda Bosne i Hercegovine d.d. - Sarajevo	Supplies	Negotiated	Rudnik mrkog uglja Breza	15,747,790
8	RS	Javno preduzeće "Putevi Republike Srpske"	Works	Open	Niskogradnja	15,391,747
9	FBiH	Javno preduzeće Elektroprivreda Bosne i Hercegovine d.d. - Sarajevo	Supplies	Negotiated	Rudnik mrkog uglja Đurđevik	14,994,427
10	FBiH	Javno preduzeće Elektroprivreda Bosne i Hercegovine d.d. - Sarajevo	Supplies	Negotiated	Alstom Power Systems GmbH	13,850,000

POLICY-MAKING AND CO-ORDINATION

Main Developments since the Last Assessment (May 2010)

There has been no concrete change in the policy-making and co-ordination system in Bosnia and Herzegovina (BiH) since the last assessment. At the time of writing (April 2011), the political crisis continues: no government (Council of Ministers) at the State level has been formed since the elections of October 2010 and the 2011 budget for the BiH state has still not been agreed.

The main development in 2010 was the award of a contract for the project (the “blueprint project”) to assist in the centre of government (CoG) reform, the implementation of which started in July 2010. A two-year contract was signed to implement jointly with the state, entities and Brčko District the agreed reform of their centres of government. However, due to a variety of problems with the performance of the contractor and to the continuing political crisis, progress has been extremely limited. The four government secretaries continue their strong support for the project, and the appointment of a new project team leader in March 2011 gives some hope that progress will be achieved in the coming months.

In the area of European integration, the most significant development was the ratification of the Stabilisation and Association Agreement (SAA) with BiH by all EU Member States. However, the European Council has not yet issued its Decision in this regard. The Interim Agreement is being implemented through the meetings of the common bodies of the state, entities and Brčko District, in which the Directorate of European Integration (DEI) is playing a key role.

In 2010 the DEI initiated a fundamental review of the co-ordination mechanisms for managing the EU accession process, with a view to improving performance and addressing present and future requirements. Following a thorough assessment of current co-ordination mechanisms and consultations with relevant state, entity and Brčko District institutions, a draft Decision on a revised co-ordination process has been prepared. The new proposal for a Decision on co-ordination will be submitted to the Council of Ministers for adoption following additional consultations. As this is still work in progress, it is not possible to assess whether or not the new approach would be an improvement over the present one.

Main Characteristics

Policy-making in general and the European integration process in particular continue to take place within a complex constitutional context, which is itself still subject to debate. The policy management system at all levels (the state and the two entities) has remained in transition, and concrete reform, although agreed in principle, has in practice been slow and uncertain. There are nevertheless foundations on which to build, such as the legal framework for policy-making and the continuing commitment of the top officials to adopt proposals that would strengthen the CoG.

There is capacity to provide logistical support for the sessions of the CoM (or governments in the case of the entities), including distribution of materials, recording and distributing decisions. There is also

some capacity to provide legal analysis and ensure conformity with the Constitution and other legislation. However, the three CoGs lack capacity to fully implement the respective Rules of Procedures, and do not have the necessary resources and competences to ensure that the rules for preparing documents for decisions are fully enforced. There is limited capacity for strategic and policy advice in the three CoGs, and such capacity is placed almost entirely with political advisers. The DEI has solid foundations and capable staff, and it is working to improve its capacity.

There are basic processes for planning the work of the CoM and the entity governments, however annual planning is still primarily a bottom-up process with variable quality. The weaknesses in inter-governmental coordination and policy-making capacities are topped up by the lack of effective medium-term financial planning. Regarding medium-term planning, an initiative in 2008 by the Directorate of Economic Policy, placed directly under the Chair of the Council of Ministers (CoM), already led to the preparation of a National Development Strategy.

Legal requirements for inter-ministerial consultation exist in all three Rules of Procedures, but they are relatively minimalist in terms of coverage and scope. They tend to require formal opinions rather than encourage discussion. In practice, policy development and law drafting capacities in ministries are weak and the incentives for inter-ministerial consultation are insufficient. The Rules of Procedure of the CoM and the entities do not require that ministries proposing materials for a decision conduct an impact assessment.

As the policy system is interlinked across governments, the existence of the Memorandum on Mutual Co-operation and of the agreement on a joint reform programme is helpful. However, policy and co-ordination capacities in the government secretariats and in ministries are still insufficient, and the expectations that the “blueprint” project would help to develop these capacities have so far remained largely unfulfilled.

Reform Capacity

In the area of policy-making and coordination, capacity for reform is constrained by the complex nature of the state, and the unfinished business of constitution building, which leads to the overall difficulties in co-operation between the governments of the state and the entities. Reform initiatives tend to become ideological and highly politicised. In the short and medium term, the reform agenda may be interrupted also by the lack of agreement on how to finance the state institutions.

However, at top official level (government secretaries), there is clearly an interest in reform, a good understanding of the shortcomings of the system, and a clear willingness and reasonable capacity to undertake reform projects together with donors. Government secretaries have remained in their positions for many years. This suggests some prospect of hope for continuity. The continuing active support of government secretaries and senior staff for the “blueprint” project, which involves significant reform of the Rules of Procedures and the CoG structures, personnel, and work processes, demonstrates this interest and commitment.

Nevertheless, unless the more fundamental constitutional and state building issues are resolved, only limited and often technical reforms, with no impact on the overall way of policy making in BiH, can be implemented. Donor involvement and other forms of international support remain critical for progress and success in the next few years. It is well known that reform of the policy system is a long-term process, and the fact that donors appear to be committed to support lasting at least four years is a positive factor.

The role of the National PAR Co-ordinator (PARCO) in ensuring progress in this area remains crucial, but PARCO will need further support in order to perform this role effectively. At present, PARCO does not have enough capacity to manage and monitor the blueprint project.

Recommendations

It is recommended that the European Commission continues to support the joint implementation by all governments of the blueprint project, and that the Commission make funds available for Phase 2 starting in mid 2012. Serious involvement of the Commission in designing and monitoring Phase 2 will be required so as to avoid some of the difficulties encountered during Phase 1.

Provide support to the European Integration process paying close attention to the new proposal for a Decision on co-ordination to be submitted to the Council of Ministers in the coming months.