

**Vision 2020**  
**Bosnia and Herzegovina**  
**Towards Its European Future**

**Sasha Toperich**  
**Heidi Obermeyer**  
**Tea Ivanovic**  
*Editors*

Center for Transatlantic Relations  
The Paul H. Nitze School of Advanced International Studies  
Johns Hopkins University

Sasha Toperich, Heidi Obermeyer, and Tea Ivanovic, eds., *Vision 2020: Bosnia and Herzegovina Towards its European Future*

Washington, DC: Center for Transatlantic Relations, 2017.

© Center for Transatlantic Relations, 2017

**Center for Transatlantic Relations**

The Paul H. Nitze School of Advanced International Studies

The Johns Hopkins University

1717 Massachusetts Ave., NW, 8th Floor

Washington, DC 20036

Tel: (202) 663-5880

Fax: (202) 663-5879

Email: [transatlantic@jhu.edu](mailto:transatlantic@jhu.edu)

<http://transatlantic.sais-jhu.edu>

ISBN: 978-0-9907721-0-1

# Contents

Preface .....	v
Acknowledgements .....	vii
List of Abbreviations .....	ix
Introduction .....	xi
<i>Lars-Gunnar Wigemark</i>	
<b>Part I: Economic and Social Reforms: Path Towards the European Union</b>	
Chapter 1 .....	3
<b>Reform Agenda for Bosnia and Herzegovina: Conception and Early Progress</b>	
<i>Gary O'Callaghan and Adnan Muminović</i>	
Chapter 2 .....	35
<b>Bosnia and Herzegovina: Reform Agenda and the Effects of its Early Implementation Phase</b>	
<i>Goran Mirašćić</i>	
Chapter 3 .....	53
<b>Financial Reforms in the Federation of Bosnia and Herzegovina as an Incentive for Economic Development</b>	
<i>Jelka Milićević</i>	
Chapter 4 .....	63
<b>Cost-Benefit Analysis of the Establishment of the Ministry of Agriculture, Food, and Rural Development of Bosnia and Herzegovina</b>	
<i>Sanela Klarić, Mubidin Zametica, Emir Klarić, Selma Osmanagić Agović</i>	
Chapter 5 .....	103
<b>Reforms in the Banking Sector</b>	
<i>Edin Karabeg</i>	
Chapter 6 .....	119
<b>Overcoming Obstacles to Land Registration Reform in Bosnia and Herzegovina through Problem-Driven Iterative Adaptation</b>	
<i>Sean Parramore</i>	

**Part II: Institutional and Political Reforms**

Chapter 7 .....147  
**How to Reform the “Reformers”?**  
*Srdjan Blagovčanin*

Chapter 8 .....153  
**The Reform Agenda and Beyond: Transitional and Structural Reforms for the New Generation of Bosnia and Herzegovina**  
*Adis Arapović and Adisa Omerbegović*

Chapter 9 .....177  
**Challenges and Expectations for Reform Activities in Bosnia and Herzegovina: The Perspective of Republika Srpska**  
*Darko Milunović and Boris Tučić*

Chapter 10 .....191  
**Reform Process in Bosnia and Herzegovina: For Youth and With(out) Youth?**  
*Ajka Baručić*

**Part III: Electronic Payments and Other Reforms**

Chapter 11 .....213  
**Energy Efficiency Investment Benefits and How to Achieve Them: The Energy Efficiency Obligation (EEO)**  
*Jane Wilson and Mak Kamenica*

Chapter 12 .....231  
**A Cashless Society is a Fairer Society: Reducing the Shadow Economy Through Financial Inclusion and the Promotion of Electronic Payments**  
*Artur Turemka*

Chapter 13 .....243  
**Bringing Bosnia and Herzegovina to the Global Tourism Market: Reforms for A Better Future**  
*Dejan Radmilović*

Chapter 14 .....259  
**The IT Sector and How to Improve the Legal Framework in Bosnia and Herzegovina**  
*Armin Talić and Marko Šiniković*

**About the Authors** .....269

## Preface

In November 2014, Germany and the United Kingdom launched a new policy initiative intended to facilitate structural socio-economic reforms for Bosnia and Herzegovina (BiH) that could be supported by the EU and endorsed by the entire political spectrum in BiH. The new EU strategy—a Reform Agenda for BiH—focused on the modernization of the labor market, with the goal of dismantling the strong grip of the country’s political elite over the economy through transparent privatization, firm conditionality from the international financial institutions (IFIs), especially the International Monetary Fund (IMF), and to support private sector growth, to create more jobs and to reduce high unemployment.

This new comprehensive EU strategy came after violent protests took place in BiH in February of 2014, injuring hundreds of people. Government buildings were set on fire, and people demanded jobs, rebuking the political elite for their inability to move the country forward.

The Reform Agenda is arguably the first successful attempt to bring both the entire international community and the political parties in BiH to some sort of consensus since the end of the war in 1995.

Even though the Reform Agenda does not address much-needed institutional reforms in BiH, nor is it meant to address the Sejdic-Finci European Court of Human Rights ruling, it does represent a significant breakthrough in bringing other crucial reforms to life.

Reforms are always difficult and require a great deal of compromise, good will, hard work, and dedicated effort. The lack of a strong and unified international policy for BiH for too long provided *carte blanche* for the corrupted political elite of the country to maintain *status quo* that benefitted only the selected few.

---

<sup>1</sup> The ruling requires BiH to amend the current constitutional arrangements of the House of Peoples and the Presidency of Bosnia and Herzegovina, which exclude minorities from being elected to office, a privilege that is only reserved for ethnic Bosniaks, Serbs, and Croats.

In this publication, our authors chart the progress that has been made, identify obstacles that still remain, highlight failures, and recommend ways to move forward.

*Daniel S. Hamilton*

Austrian Marshall Plan Foundation Professor  
Executive Director, Center for Transatlantic Relations

*Sasba Toperich*

Senior Fellow, Center for Transatlantic Relations SAIS  
Director, Mediterranean Basin Initiative

## Acknowledgments

This publication would not have been possible without the support and input of our colleagues at the America-Bosnia Foundation, in particular Mak Kamenica, Executive Director, and Dejan Radmilović, Project Manager.

We wish to express special thanks to H.E. Ambassador Lars-Gunnar Wigemark for writing the introduction and to the EU Delegation in Bosnia and Herzegovina for their partnership in this effort.

We are also thankful to the Sarajevo Canton for their ongoing support towards our “Vision 2020” program designated to support the ongoing Reform Agenda in Bosnia and Herzegovina. We thank the World Youth Leadership Network (WYLN) for their support.

Our gratitude goes out to the government of the Federation of Bosnia and Herzegovina for their support on this project.

Our thanks also go out to Andy Mullins, CTR–SAIS Non-resident Fellow and Board member of the America–Bosnia Foundation for his edits in the last phase of production.

As always, we are grateful to Peggy Irvine and Peter Lindeman for working out the publishing details of this and many other CTR publications.

The opinions expressed in the following chapters are the authors’ alone, and do not necessarily represent the views of any government or institution, or those of their fellow contributors.

*Tea Ivanovic*

Fellow, Center for Transatlantic Relations SAIS

*Heidi Obermeyer*

Fellow, Center for Transatlantic Relations SAIS

*Sasha Toperich*

Senior Fellow, Center for Transatlantic Relations SAIS



# Abbreviations

APHP	Administration of Bosnia and Herzegovina for Plant Health Protection
BAM	Bosnia and Herzegovina Convertible Mark (currency)
BD	Brčko District
BiH	Bosnia and Herzegovina
CAP	Common Agricultural Policy
CBA	Cost–Benefit Analysis
CD	Certificate of Deposit
CPI	Corruption Perception Index
CPS	Country Partnership Strategy
CRPC	Commission for Real Property Claims of Displaced Persons
CSO	Civil Society Organizations
DPL	Development Policy Loan
EY	Ernst & Young
FBIH	Federation of Bosnia and Herzegovina
FDI	Foreign Direct Investment
FIRR	Financial internal rate of return
FNPV	Financial net present value
UHIRBiH	Association of Hoteliers and Restaurateurs of BiH
UTABiH	Association of Travel Agencies of BiH
RS	Republika Srpska
AKP	Justice and Development Party
BIGMEV	Development Center of Cultural, Economic, and Scientific Relations
BiH	Bosnia and Herzegovina
CEFTA	Central European Free Trade Agreement
CEPS	Centre for European Policy Studies
EBRD	European Bank for Reconstruction and Development
EE	Energy Efficiency
EEO	Energy Efficiency Obligation Scheme
EFF	Extended Fund Facility
EIB	European Investment Bank
EnC	Energy Community
ERP	Economic Reform Programs
EU	European Union
EUSR	EU Special Representative in Bosnia and Herzegovina
FAC	Foreign Affairs Council
FDI	Foreign Direct Investment
FMAWF	BiH Federal Ministry of Agriculture, Water Management, and Forestry
FSA BiH	Food Safety Agency of BiH
FYROM	Former Yugoslav Republic of Macedonia
FX	Foreign Exchange Risk
GAC	General Affairs Council
GCI	Global Competitiveness Index

GDP	Gross Domestic Product
GIZ	German Society for International Cooperation
IBM	Integrated Border Management
IEA	International Energy Agency
IFI	International Financial Institution
IFOR	Implementation Force
IMF	International Monetary Fund
IPA	Instrument for Pre-accession Assistance
IPARD	Instrument for Pre-Accession Assistance in Rural Development
KM	Convertible Marks (Bosnian currency)
KM	Kilometers
MAP	Membership Action Plan
MAFWM-RS	Republika Srpska's Ministry of Agriculture, Forestry, and Water Management
MoFTER BiH	Ministry of Foreign Trade and Economic Relations of BiH
NATO	North Atlantic Treaty Organization
NPL	Non-Performing Loans
OHR	Office of the High Representative
OIC	Organization of Islamic Cooperation
PAR	Public Administration Reform
PDIA	Problem-Driven Iterative Adaptation
PEIR	Public Expenditure and Institutional Review
PFM	Public Financial Management
PIC	Peace Implementation Council
PKK	Kurdistan Workers' Party
RA	Reform Agenda
REC	Real Estate Cadastre
RCC	Regional Cooperation Council
RSGA	Republika Srpska' geodetic authority
RYCO	Regional Youth Cooperation Office
SAA	Stabilization and Association Agreement
SBA	Stand-By Arrangement
SCO	State Certification Officer
SEEBRIG	South-Eastern Europe Brigade
SFOR	Stabilization Force
SIPA	State Investigation and Protection Agency
SLDC	Solution and Leadership-Driven Change
SME	Small and Medium Sized Enterprise
SOE	State-owned Enterprises
SVO BiH	State Veterinary Office of BiH
TIKA	Turkish Cooperation and Coordination Agency
UN	United Nations
UNDP	United Nations Development Program
VAT	Value Added Tax
WEF	World Economic Forum
WB	Western Balkan(s)

The editors would like to also note the following (as of September 1, 2017):

1 BAM equals 0.60 U.S. dollars

1 euro equals 1.18 U.S. dollars

## *Introduction*

# **The Reform Agenda at Halftime**

*Lars-Gunnar Wigemark*

Working on the Reform Agenda, with the people and authorities of Bosnia and Herzegovina, has been one of the great challenges and pleasures of my professional life. With the publication of this book, we have an opportunity to pause, reflect, and to consider what lessons can be drawn from the last two years as we go into the final stages of planned reforms.

The origins of the Reform Agenda lay not so much in the social unrest of 2014 as the underlying harsh reality for many citizens in BiH: too few jobs, for too little pay, dependent on political connections, while a privileged few enjoy the benefits and security of employment. Such an unequal and unbalanced system and frustration born of it, is what drives too much of Bosnia and Herzegovina's talent outside of its borders every year. In one important aspect, the Reform Agenda has already fulfilled a major part of its purpose—for the first time in the post-war history of BiH, socio-economic reforms are at the center of local and international efforts.

For far too long, the country's clear desire to progress towards European Union membership was frustrated, by in-fighting, a seemingly perennial political crisis, and constitutional, perhaps even existential, conditions. The Reform Agenda is an essential part of a redefined and reinvigorated approach on the part of the European Union towards Bosnia and Herzegovina, putting some of the intransigent political or legal obstacles aside in order to focus on urgent economic and social changes needed to make a real difference in the daily lives of BiH citizens. The General Affairs Council decision of September 2016 to begin the Commission Opinion process, and the presentation to BiH of the Questionnaire in December 2016, have helped us to get going on the EU path once again.

But this is not the EU's Reform Agenda, or the international community's. It belongs to the citizens of the country, as a commitment made by their political leaders, to change the fundamental nature of the way the country works. In short, a country that has unleashed the potential of its private sector, while reducing the footprint of the excessive public sector, and a country that has shifted its inward focus from local consumption

and imports towards international integration, investments and exports. Ultimately, this would lead to a situation where more people can find the opportunity and rewards they deserve, in a safe and just environment.

The international financial institutions and the EU put together a generous package of financial assistance for the Reform Agenda. Direct budget support from the IMF, the World Bank, and the EU is expected to deliver 850 million euros over three years. Additional support for infrastructure development and private sector investment could bring total international assistance to 1.5 billion euros. From the outset, the United States lent political support to this joined up approach and engaged actively to back the Reform Agenda.

Two years later, it is natural to review progress. Until recently, and in terms of adopted measures, BiH was largely on track, although we have seen a disappointing loss of momentum in recent months. New laws have been adopted to improve the labor market and fight the gray economy, to strengthen the banking sector; to make the pension system more fair and sustainable, to sort out public finances, and to create a better business environment. There are, of course, many challenges ahead, including ensuring full implementation of these changes, public sector restructuring, health care reform, lowering the tax wedge of labor, and much more.

I sometimes hear doubts, understandable ones, if these new laws and rules will make any real difference to the country. But they already are making a difference. To take a concrete example, the adoption of a pharmaceutical rulebook in November, something I am confident would never have been achieved without both the carrot and stick of the Reform Agenda, will lower the costs of medicines for every citizen in BiH. But we have also seen the ability of short-sighted politicking and party interest to block vital reforms, including an excise package that would have unblocked 1 billion euros in essential road and highway investments. I am convinced, however, that these are temporary setbacks and reforms need to continue.

Real change is made on the ground. In the Sarajevo Canton, for example, both costs and waiting times for business registration have been reduced and the canton recorded an increase of almost 20 percent in newly registered businesses—proof that reforms pay off. These measures should soon be mirrored in other cantons and the city of Banja Luka has embarked on a similar project. But what can we say of the aim of the Reform Agenda to change the big, macro-economic picture?

Although structural reforms take time, generally much longer than 18 to 24 months, we can already identify some positive indicators that justify our efforts and optimism: Industrial production increased by 7.3 percent in the last year. Mining and manufacturing recorded modest growth in 2016 and there was a significant increase in energy generation. As this book goes to print, exports increased by 14 percent over the last twelve months, led by the automotive industry, furniture and wood processing, footwear, aluminum, iron, and electricity production. Retail sales are rising quickly and tax revenues reached record heights in 2016. Banks in the Federation of Bosnia and Herzegovina (FBiH) have started lending more aggressively, up 10 percent since 2015, and enterprise deposits in banks jumped in 2016, probably reflecting greater profitability. Most importantly, the number of registered unemployed citizens decreased while the number of registered employed people increased, and those new jobs were generated in the private—not the public sector. The preliminary results of the 2017 Labor Force Survey show that the unemployment rate is down to 20.5 percent from 25.4 percent last year. Although mainly due to a decrease in the labor force (ageing population and emigration), employment increased by 2 percent and it cannot be denied that the Reform Agenda has started generating jobs.

The process we are promoting jointly with local authorities, the International Financial Institutions, and major partners such as the United States was never going to be an easy one, and we are always bound to face delays and resistance, especially from the privileged few. However, our benchmark for success is to improve the lives of the majority of citizens and the above gives us reason to hope and continue to jointly fight for reforms.

And so, to this timely and welcome collection. Gary O’Callaghan and Adnan Muminović have led much of the EU engagement with the Reform Agenda. In their chapter “A Reform Agenda for BiH: Conception and Early Progress,” they set out the fundamental parameters of the program and describe how it was put together.

Much of the action for the Reform Agenda lies with the entities. On the FBiH side, the example has been set from the top, with Prime Minister Fadil Novalić, his senior economic adviser, Goran Miraščić and Minister of Finance Jelka Milićević. In his chapter, Miraščić explains the need for change, the baseline from which the subsequent reforms would build. Minister Milićević highlights the importance of investments and private sector entrepreneurship as the engines for job creation and economic

development. Boris Tučić and Darko Milunović, of the Republika Srpska (RS) Prime Minister's Office, share their perspectives on how the Reform Agenda supports and reinforces the development priorities of the government in Banja Luka. In doing so, they also present an answer to the question, "Why invest in Republika Srpska?"

As I tour around BiH to discuss the path to EU membership, and the Reform Agenda, a consistent theme of the questions I receive is what it will all mean for agriculture and food production. This should be one of the country's strongest sectors, and still has enormous potential. In their chapter, Sanela Klarić, Muhidin Zametica, Emir Klarić, and Selma Osmanagić Agović provide a thoughtful analysis of what a state level ministry would be able to achieve for agriculture, food, and rural development. These debates are always worth having.

The banking sector can and must play a central role in securing of domestic and foreign investment in the country. In his contribution, Edin Karabeg offers us a banker's perspective on the kinds of economic and political changes needed ahead, to improve the country's rating, modernize infrastructure, and enhance both tax and labor systems.

Meanwhile, Sean Parramore of Queen Mary University in London focuses on a different kind of obstacle, the country's chaotic land registration system, and how it might be reformed. While there is some recent progress to report, he helpfully highlights the risks that incomplete changes risk benefitting only a narrow elite and increasing the potential abuse of power.

In the second part of the book, the focus moves to institutional and political reform. Tackling the systemic basis for corruption, a blight on the business climate and handbrake on growth in BiH, is the focus of Srdjan Blagovčanin's chapter, "How to reform the 'reformers?'" He rightly identifies that current elites, with their vested interests, will naturally seek to oppose change and defend the status quo.

The Reform Agenda too must be open to challenge and scrutiny, and I regularly appear at events, on television, and in print to discuss and explain the rationale of the program. Adis Arapović and the Center for Civic Initiatives, have helped to lead and direct exactly that kind of debate. In their chapter, Adis Arapović and Adisa Omerbegović set out some of the political and historical context, and the current challenges BiH faces. They encourage us to look further, to a "Vision 2022" which will draw the country closer to EU, NATO, WTO, and other global associations.

In the context of the Reform Agenda, I often find myself talking about, or better with, young people in BiH. Given the still unacceptable levels of unemployment they face, they are the ones most likely to benefit from the long-term changes the program hopes to achieve. In a chapter titled “The Reform Process in BiH—for youth and with(out) youth,” Ajka Baručić helps us to understand them, the problems they encounter, and what this might all mean for the persistent brain drain of the country’s best and brightest.

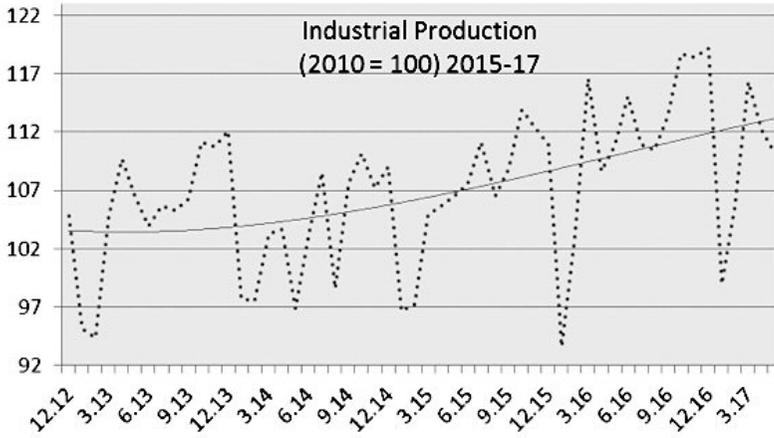
The third section of the book takes a different approach, focusing on individual sectors or processes which can support, or be supported by, the reform process. Jane Wilson and Mak Kamenica make a convincing case for the multiple hidden benefits of increased energy efficiency, quantifying the far-reaching impact that it could have on SMEs development, new employment, energy savings and air pollution reduction.

Artur Turemka, of Mastercard, shares a corporate analysis on BiH and the benefits of further movement towards a cashless society. The country’s shadow economy is well-documented, resulting in billions of euros in lost tax revenue, accounting for perhaps as much as 25 percent of GDP. Addressing the “financially excluded,” especially young people, Turemka argues, could provide benefits for both consumers and governments in BiH.

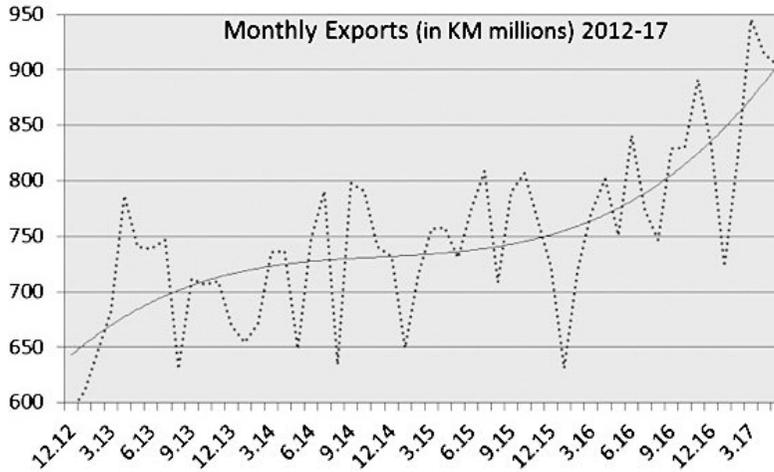
Dejan Radmilović reveals the tremendous capacity for the growth and development of BiH’s tourism sector due to its unique combination of natural resources and a rich cultural heritage. The sector could become a major driving force for the economy, allowing other industries in the country to grow and develop through the fresh capital pouring in. This would also allow for easier implementation of reforms and could contribute to the development of both the country as a whole, as well as local communities.

In a fascinating analysis of the potential for BiH’s IT sector, BIT Alliance explains how to strengthen this most strategic, and forward-looking of sectors. The shortfall in training software engineers is just one symptom of the gap between what BiH’s education system is producing, and what it needs to compete and get ahead.

I would like once again to thank all of the contributors, and those responsible for bringing this book together. There is still a good way to go in the Reform Agenda, and Bosnia and Herzegovina’s progress towards the European Union, but I remain confident that working together we can jointly realize that goal.



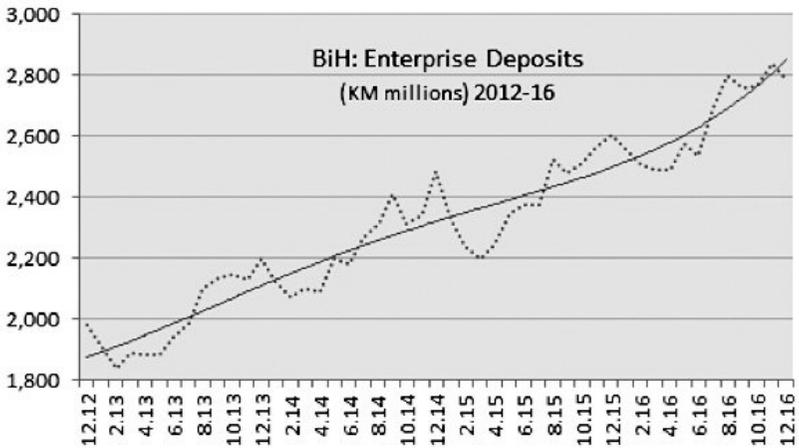
Source: Compiled Monthly Data from the BiH Agency for Statistics



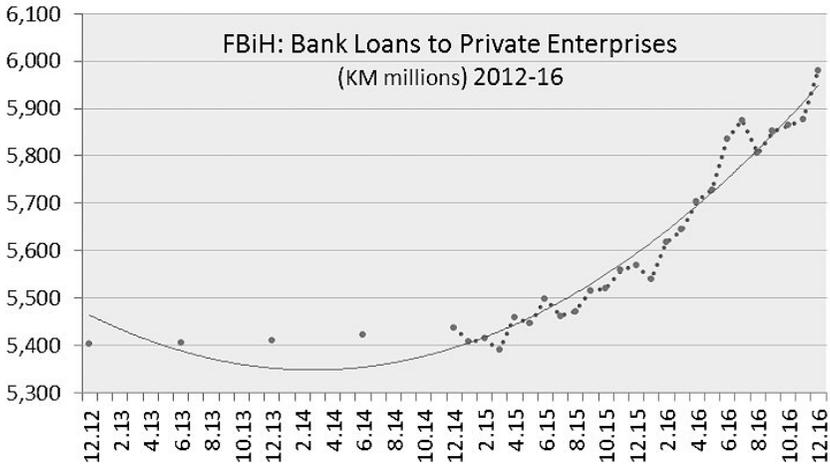
Source: Compiled Monthly Data from the BiH Agency for Statistics



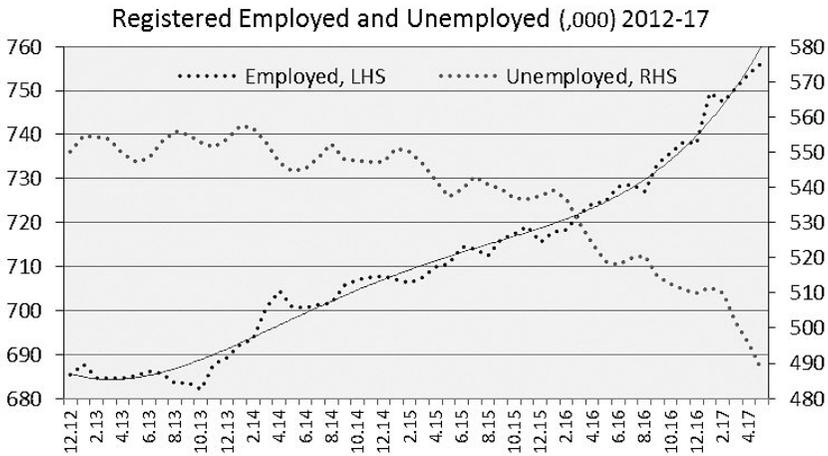
Source: Compiled Monthly Data from the BiH Agency for Statistics



Source: Central Bank of Bosnia and Herzegovina, Bulletin 2 2016



Source: Central Bank of Bosnia and Herzegovina, Bulletin 2 2016



Source: Compiled Monthly Data from the BiH Agency for Statistics

*Part I*

**Economic and Social Reforms:  
Path Towards the European Union**



## *Chapter 1*

# **Reform Agenda for Bosnia and Herzegovina: Conception and Early Progress**

*Gary O'Callaghan and Adnan Muminovic*<sup>1</sup>

Socioeconomic and related reforms were long delayed in Bosnia and Herzegovina (BiH) and, as each year passed, the economy fell further behind its neighbors in terms of the business environment and the policies necessary to spur investment and create jobs. As a result, the overall unemployment rate stands at over a quarter of the workforce and the rate of youth unemployment is among the highest in Europe. A bloated government sector cannot deliver basic services and moribund public enterprises distort opportunities in the economy.

Social disturbances at the beginning of 2014 highlighted the fact that urgent reform was necessary. But the people of BiH had been listening to the cry for reform for many years and, despite the rhetoric, nothing significant had changed. The challenge for the international community was to convince the public and the authorities that true reforms could deliver prosperity, jobs and greater opportunity. The challenge was met by agreeing on a set of priority measures that would re-ignite the process of modernizing the economy. This Reform Agenda would, it was hoped, create growth and generate further momentum for change.

The Reform Agenda emerged in mid-2015 from an eighteen-month process of consultation and negotiation that reflected the European Union's renewed emphasis on socioeconomic and related reforms in BiH. The authorities took ownership of the Agenda during the negotiation process and this has been crucial to the progress achieved. Meanwhile, the European Union (EU) and International Financial Institutions (IFIs) agreed that—based on their experience with disappointing reform programs in 2009–2014—no financial assistance would be available until a significant commitment to reforms had first been demonstrated. This

---

<sup>1</sup> Any opinions expressed do not necessarily represent the opinion of the EU or EUSR. The authors would like to use this opportunity to thank their colleagues from the EUSR and EU Delegation in Bosnia and Herzegovina for their valuable input and contributions to this paper, in particular our former colleagues Dr. Renzo Daviddi and Thomas Busch who were instrumental in getting the Reform Agenda adopted and launched.

strategy—to insist on reforms before financial support was disbursed—has also been productive.

The authorities' commitment to reforms put them back on the road to EU accession and bolstered political support for some difficult measures. In addition, the Reform Agenda benefitted from an unprecedented degree of cooperation between the EU and IFIs. Different institutions assumed responsibility for leading assistance to reforms in various areas, but these efforts have been fully consistent with one another and properly harmonized. The EU and IFIs are supporting the authorities' Agenda with a well-sequenced package of measures and, if it is to succeed, this package must be implemented in full: from an economic perspective, jobs need to be created in the private sector if the public sector is to be downsized; and, from a social perspective, the creation of opportunities for the young must be combined with adequate concern for the dignity and comfort of the elderly.

After protracted negotiations and the implementation of a series of early reforms (including long-delayed labor laws and the liquidation of some bankrupt banks), the IMF approved a three-year arrangement under its Extended Fund Facility (EFF) in September of 2016. The World Bank approved an Employment Project in January 2017 and a Development Policy Loan (DPL) in March 2017 (after securing other reforms including long-overdue limits on pharmaceutical prices). These flagship programs guide assistance to the socioeconomic aspects of the Reform Agenda and are designed to facilitate the provision of 800–850 million euros in direct budget support from the EU and IFIs during 2016–2019. A further 500 million euros in investment, largely in infrastructure, is expected to follow. They also provide the umbrella for a set of subsidiary programs and technical assistance. Meanwhile, the EU is leading efforts to secure meaningful reforms to the rule of law, governance and public administration.

## **Background and Approach to Reform Agenda**

### *Recent Experience with Reform Programs*

Two sets of reform programs in 2009–2014 did succeed in preserving financial stability in BiH after the global financial crisis, but they did not achieve significant structural reforms. The IMF, EU, and World Bank made significant resources available for a worst-case fallout from the global financial crisis but, as it turned out, the crisis in BiH was not as severe as it might have been. Meanwhile, the authorities were content to accept the

cash that was available at the beginning of each program, but never undertook the structural reforms that were delayed to the end of each. Neither set of programs was fully completed.

The two programs did help BiH survive through a very difficult period that began in 2009. Real economic growth averaged almost 6 percent per annum during 2005–2008 but turned sharply negative (3 percent) in 2009 and recovery was sluggish through 2014. In these circumstances—and in the context of severe floods that hampered growth and amplified budget deficits in 2014—a rising government deficit was twice corrected and set on a downward path. Fiscal stability was maintained and the banking sector was not undermined.

However, the experience with structural reforms was mixed at best. In 2011, a review of the World Bank Country Partnership Strategy (CPS, for 2008–2011) concluded that its assistance:

[...] partially succeeded in accelerating corporate restructuring and privatization, and had marginal success in improving the business climate. [It] helped deliver better municipal services and primary healthcare ... but the targeting of social services did not improve as expected under the program. Moreover, contrary to program objectives, government spending as a share of GDP increased ... while fiscal coordination among the entities that make up BiH suffered setbacks. The overall program [was deemed] *moderately satisfactory*.<sup>2</sup>

The 2011 review recommended that the World Bank explore ways of dealing effectively with what it saw as the main problem—political stalemate between the entities.

The IMF also struggled to make progress on structural reforms and there was significant policy drift after October 2010 elections that “weakened the national policy coordination needed to design an effective response to the emerging challenges.”<sup>3</sup> By the time the next review of progress (of the CPS for 2012–2015) came around in 2014, the World Bank still concluded that “political fragmentation and stalemate [had] undermined reform processes.” “The authorities [had] failed to advance sensitive reforms of social and veteran benefits that would have improved the quality of spending.” Consequently, the World Bank cancelled a series

<sup>2</sup> World Bank Group. 2011. *BiH-Country Assistance Strategy Completion Report Review for the Period FY2008-11*: IEG review. p.1.

<sup>3</sup> IMF. 2011. *Press Release No.11/426: Statement by the IMF Staff Mission to BiH*.

of planned public expenditure reforms (DPLs)—aimed at reforms to the civil service, pensions, and social benefits—and switched its focus to support for the business environment (that would be less politically sensitive). Meanwhile, it noted that “political fragmentation and stalemate remain the principal risks for delivery of the program.”<sup>4</sup>

This experience during 2009–2014 led to the following conclusions:

- There was a need to link reforms to disbursements, including front-loading reforms in future programs and delaying financing until reforms are enacted.
- There was a need to cultivate a shared sense of ownership of reforms across both entities.
- There was a need for close cooperation and coordination between the EU and the IFIs.

#### ***2014: A New EU Approach and International Coordination***

In early 2014, there was a set of sustained public disturbances in BiH that demonstrated public frustration with the overall state of the economy and social services. These triggered significant political concerns but also presented an opportunity to try and change the political atmosphere in the country.

At the same time, the EU adopted a renewed focus on implementing economic reforms, improving economic governance and focusing on structural impediments to growth across the countries of the Western Balkans (WB). In its Enlargement Strategy for 2014–2015, the European Commission identified economic governance as one of the key challenges for the WB countries on their path towards EU accession. It recognized that these countries faced the major structural economic challenges of high unemployment, low foreign direct investment and low levels of competitiveness. Moreover, weaknesses with the rule of law and public financial management (PFM) exacerbated the risk of corruption and negatively impacted good governance of the economy and the investment climate. It noted that none of the WB countries had yet met the Copenhagen economic criteria.<sup>5</sup> It was clear that the new approach was particularly appropriate and urgent for BiH.

---

<sup>4</sup> World Bank Group. 2014. *Country Partnership Strategy Progress Report for BiH for the Period FY12-FY15*, p.2.

<sup>5</sup> European Commission. 2014. *Enlargement Strategy and Main Challenges 2014-15*.

In this context, the EU and IFIs launched an initiative to draft a *Compact for Growth and Jobs* that would aim to identify and build support for a package of 5–6 concrete measures intended to re-ignite the process of modernizing the economy. The *Compact* would be drafted in ample time to inform the election campaign of October 2014 and would be presented to the citizens of BiH as a concrete and significant step toward a brighter future. It would seek to address many of the concerns that had been expressed during the public disturbances and would be widely publicized. Reforms would be presented in a manner that was clearly related to improving people’s lives.

The development of the content of the *Compact* was discussed and coordinated between the EU, IMF, World Bank Group and EBRD. This gave operational content to an earlier agreement between the EU and IFIs at a High-Level meeting in November 2013 to jointly review their policies and strategies. The *Compact for Growth and Jobs in BiH* would allow them to implement a joint commitment to increase “cooperation on the ground” while allowing each IFI to operate “within the remit of the respective mandate of each institution.”<sup>6</sup>

The content of the *Compact* would be kept to a bare minimum so that the essential priorities for reform would get the full attention of policy makers and the public. They would be explained in simple terms and not complicated by too many elements. At the same time, it would be important to build significant local political ownership of the agenda for reform. Of course, it was clear from the outset that this would take time.

### ***A Compact for Growth and Jobs: Focus on Inclusion and Local Ownership***

A package of six urgent reform priorities was chosen at the *Forum for Prosperity and Jobs* in May of 2014, which was attended by a broad spectrum of civil, academic, business and political society in BiH. It was supported by the EU and IFIs—and by others in the international community. Further consultations with local, regional and international experts, as well as on the social media, produced a final package—a *Compact for Growth and Jobs*—that was launched in July 2014. The main measures focused on lowering the tax wedge on labor and other labor market reforms; improvements to the business climate as measured by the World Bank’s *Doing*

---

<sup>6</sup> *Joint Conclusions* of the High-Level meeting between the European Commission and Financial Institutions on the Western Balkans from 5 November 2013.

*Business Report*; the restructuring of state-owned enterprises (SOEs); fighting corruption; and improved targeting of social protection.

A full-scale public relations campaign—launched with the support of Norway—encouraged the public to support change and encouraged the political leadership to embrace reforms. Political parties were urged to endorse the *Compact* prior to upcoming elections and the campaign had a marked influence on election results. New governments designed their programs around many of these themes.

Meanwhile, in December 2014, the Foreign Affairs Council (FAC) of the EU urged for rapid reform progress by incoming governments, which would make a real difference to the lives of ordinary citizens and re-energize BiH's European path. They suggested that, in return for a promise of reforms, the FAC would consider implementing BiH's Stabilization and Association Agreement with the EU (that had been suspended for eight years). They asked for a written pledge from political leaders to pursue reforms and this was delivered in January of 2015. The FAC noted that "meaningful progress" with the *Compact* agenda would be necessary for an EU membership application to seriously be considered.

## **Choosing Priorities for Reform**

The FAC Conclusions of December 2014 made clear that, before it could join the EU, BiH would have to demonstrate that it had a functioning market economy and had the capacity to cope with competitive pressures within the EU. It noted that the reform package identified in the *Compact* would help BiH get closer to EU standards in the economic sphere and urged the authorities to turn this into a reform agenda whose overall objective would be to establish functionality and efficiency at all levels of government. This agenda would also need to include complementary reforms to the rule of law and good governance.

### ***Drafting the Reform Agenda***

The newly elected governments at the State and entity levels began the process of agreeing on a Reform Agenda in early May of 2015. A high-level intergovernmental Retreat compared the three sets of programs for government and considered proposals and analysis from the IFIs and EU. Government representatives agreed that there needed to be a renewal of confidence that short-term sacrifices were worth making in pursuit of

medium-term growth and jobs. This level of trust could only be established on the basis of a firm commitment by all political leaders and institutions to comprehensive reforms.

The Reform Agenda for 2015–2018 went through thirteen drafts before it was eventually agreed in late July and this arduous process attests to the seriousness with which each measure was considered and negotiated. The process itself lent a high degree of credibility to the final product and governments adopted it with a high degree of commitment and ownership. The Agenda, as summarized in Table 1, is divided into six categories (that broadly conform to the six areas set out in the *Compact*). These are:

1. Public Finance, Taxation and Fiscal Sustainability
2. The Business Climate and Competitiveness
3. The Labor Market
4. Social Welfare and Pension Reform
5. Rule of Law and Good Governance
6. Public Administration Reform

The measures set out in the Agenda often overlap and reinforce one another in their effectiveness. And they cover a broad set of problems in the economy. More generally, governments recognized that it was important to view the Agenda as a comprehensive set of reforms that would need to be pursued as a complete package. A broad set of reforms was necessary in order to secure growth and jobs and it was also recognized that any sacrifices would need to be shared in order to ensure broad political commitment. If the Agenda was treated as a selection box—with different groups supporting different aspects—it would surely come apart and fail to deliver its goals. Moreover, the reforms would need to be properly sequenced and planned if they were to succeed. Important goals—like combating corruption and political patronage—cut across all measures.

### ***Sequencing and Momentum***

Table 1 presents the six categories of reforms in three phases—as they would be implemented over a three- to four-year period. The first phase, introduced in 2016, concentrated on those areas where reforms could be planned and implemented quickly. These were not necessarily the easiest reforms—from a political perspective—and governments agreed that it would be necessary to establish early momentum to ensure the success of the entire Agenda. Significant measures were required in order to signal

Table 1. BiH Reform Agenda – Major Themes and Sequencing

	I 2016	II 2017	III 2018	III 2019+
<b>Themes:</b>				
<b>Phases:</b>				
<b>1 Public Finance, Taxation &amp; Fiscal Sustainability</b>				
a <b>Fiscal consolidation and sustainability</b>				
• Put debt levels on a downward trajectory				-----
• Reduce current spending (especially, on wages) and create room for investment		Salary freezes and moratorium on hiring	Public-sector rightsizing and flexible wage determination	Investment with effective planning and use of PIPs
• Public investment programmes (PIPs)		Approve PIPs	Implement PIPs	
b <b>Strengthen tax collection + broaden base</b>				-----
• Strengthen revenue collection		Regular data exchange between four tax authorities and measures to broaden and harmonise tax bases		
• Broaden and simplify revenue base		Amend tax laws	Harmonise tax laws	
c <b>Improve fiscal control and responsibility</b>				
• Enhance budget/debt rules and control		New laws to strengthen control. Toughen constraints on budgets and accumulation of debt.		
• Public Internal Financial Control (PIFC)		----- Strengthen Public Internal Financial Control	-----	
• Tackle loss-making state-owned enterprises		Improve control on SOEs	Catalogue arrears in SOEs and place limits on further arrears	
d <b>Cut taxes on labour</b>				
• Amend contribution structure.		Gradually reduce taxes on labour and compensate with higher excises and broader tax base.		
e <b>Combat the grey economy</b>				
• Combat tax evasion		Improve tax procedures.	New laws and procedures on tax collection.	
• Make it easier to pay taxes		Prevent wage under-reporting and limit tax exemptions.	Introduce e-services for income taxes and VAT.	
f <b>Health reform</b>				
• Reorganise health systems		Introduce norms/guidelines.	Comprehensive health sector reforms agreed and implemented with the World Bank.	
• Improve financial controls		Introduce Health to treasury system and combat arrears.	Introduce new models of health funding.	
g <b>Debt management</b>				
• New debt management strategy.		Exchange of data on structure and composition of debt		
<b>2 The Business Climate and Competitiveness</b>				
a <b>Improve the business environment</b>				
• Attract foreign investors				
• Make it easier to do business and invest				
• Reduce local regulation and para-fiscal burden				
b <b>Strengthen investor protection</b>				
• Improve corporate governance				
• Strengthen insolvency frameworks				
• FBiH to introduce commercial courts				
c <b>Restructure State Owned Enterprises (SOEs)</b>				
d <b>Safeguard financial sector stability</b>				
• Address problem banks				
• Strengthen bank supervision				
• Adopt new banking legislation				
• Revive bank lending and liquidity				
e <b>Simplify customs procedures</b>				
• New Laws on Foreign Direct Investment and simplification of business registration.				
Prepare for one-stop-shop.		Introduce and enhance one-stop-shop.	Simplify rules and cut barriers to investment.	
Expedite permits.		registers of pair-fiscal fees.	Introduce controls/monitoring on local fees.	
New Laws on Companies and Investment.				
Shorter bankruptcy procedures.		Introduce pre-bankruptcy options.		
Undertake a Feasibility Study.		Legislate and train (also in RS).	Restructure relevant court structure.	
List viable and non-viable SOEs.		Restructure railways & mines.	Restructure and privatise other SOEs.	
Audit and liquidate banks.		Promote bank consolidation.		
Review operations of Banking Agencies and restructure and train where necessary.		Adopt harmonised banking legislation and practices in both entities, including resolution.		Consider merging Agencies.
Agree on new bank laws.		Inspections reform		
New Laws on Payments.				
Law on Customs Policy				Strengthen national quality control

Themas:	Phases:	Table 1 (concluded), BiH Reform Agenda – Major Themes and Sequencing		
		I 2016	II 2017	III 2018+
<p><b>3 The Labour Market</b></p> <ul style="list-style-type: none"> <li>a Stimulate new employment                             <ul style="list-style-type: none"> <li>• Improve flexibility, limit collective agreements and enforce workers' rights</li> </ul> </li> <li>b Encourage labour-market participation                             <ul style="list-style-type: none"> <li>• Support schemes for first-time job seekers &amp; encourage participation in labour market.</li> </ul> </li> <li>c Improve employment targeting and skills                             <ul style="list-style-type: none"> <li>• Improve mediation in labour search</li> <li>• Education linked to labour market</li> </ul> </li> </ul>	<p>Introduce new Labour Laws and Collective Agreements.</p> <p>Budget for wage subsidies. Prepare ALMP schemes.</p> <p>Delink Health and Employment. Review TVET system.</p>	<p>Reinforce labour inspections</p> <p>Support first-time job seekers. Introduce ALMP schemes.</p> <p>Improved targeting of unemployed and advertising/training. Reform of education system</p>	<p>Reinforce labour inspections</p> <p>Support first-time job seekers. Extend ALMP schemes.</p> <p>Reform of education system</p>	<p>New collective agreements</p>
<p><b>4 Social Welfare and Pension Reform</b></p> <ul style="list-style-type: none"> <li>a Ensure sustainability of pension systems</li> <li>b Improve efficiency of social welfare support                             <ul style="list-style-type: none"> <li>• Improve targeting of social assistance</li> <li>• Provide incentives to work</li> </ul> </li> <li>c Clear arrears in social funds in FBiH</li> <li>d Introduce voluntary pension systems</li> </ul>	<p>Agree/adapt new Laws in FBiH.</p> <p>Continue beneficiary audits. Review benefits/disincentives. Identify arrears &amp; legislate. Laws on Voluntary Funds.</p>	<p>Implement new Laws in FBiH.</p> <p>Establish database of beneficiaries. Introduce incentives for return to labour market. Commence arrears payments and legislate retirements. Introduce regulations.</p>	<p>Review pension sustainability in RS.</p>	
<p><b>5 Rule of Law and Good Governance</b></p> <ul style="list-style-type: none"> <li>a Judicial reform</li> <li>b Integrity and cooperation in law enforcement</li> <li>c Anti-corruption capacity building</li> <li>d Improve asset seizure</li> <li>e Money laundering and terror financing</li> <li>f Harmonize Laws on Weapons</li> <li>g Integrated border management (IBM)</li> </ul>	<p>Agree Judicial Reform Strategy. Appraise/improve cooperation. Adopt anti-corruption docs. Plan for improvements. Adopt Action Plan for FATF. Draft Laws. Agree IBM Strategy.</p>	<p>Implement Judicial Reform Strategy (and guidelines on corruption). Implement recommendations from the appraisal. Set up anti-corruption monitoring and prevention bodies. Adopt mechanisms pursuant to minimum principles. Adopt legislation in line with international standards. Adopt Laws with agreed common principles. Implement IBM Strategy.</p>		
<p><b>6 Public Administration Reform (PAR)</b></p> <ul style="list-style-type: none"> <li>a Key principles of PAR                             <ul style="list-style-type: none"> <li>• Adopt key principles of PAR</li> <li>• Reform of Public Financial Management (PFM)</li> </ul> </li> <li>b Civil service reform                             <ul style="list-style-type: none"> <li>• Introduce greater flexibility in working</li> <li>• Public sector right-sizing</li> </ul> </li> <li>c Limits on hiring and wages</li> <li>d Transparency in procurement and hiring</li> <li>e Census Implementation</li> </ul>	<p>New SIGMA baselines. Agree PFM Reform Strategy</p> <p>Amend Laws on Civil Service. Plan significant reorganization. Introduce nominal wage freeze</p> <p>Introduce Procurement Appeals. Agree and conclude.</p>	<p>Adopt new PAR Reform Strategy and adopt further principles via Special Group on PAR.</p> <p>Implement PFM Reform Strategy</p> <p>Amend working practices and compensation schemes for flexibility and incentives. Implement reorganization and restructuring of public service. Revise human resources and recruitment plans. Eligibility criteria and competence tests for civil service. Only employ the best candidates.</p>		

the fact that a serious process had begun. Also, governments noted that countries that embrace economic reforms often get significant and early benefits that can lead to a virtuous cycle of reform and growth. For example, the three Baltic countries, who initiated a second round of reforms after 2008, posted by far the strongest growth rates in the whole of the EU and Central and Eastern Europe in 2011–2014.

Other reforms would take longer to introduce and would fall into later phases. Three factors could explain why certain measures needed to be delayed:

- a. Some reforms would require a significant amount of preparation and planning before they could be launched. This applied, for example, to the need to restructure the civil service and SOEs. Nevertheless, this second set of reforms would need to be carefully planned while the first phase of reforms was being introduced so that momentum would not be lost between the different phases.
- b. Some reforms involve a significant degree of institution-building that can only take place slowly. They require that laws be adopted and technical assistance be provided so that the relevant institutions would evolve properly over time. This applies, for example, to many aspects of Public Administration Reform (PAR). But it may also be necessary to adopt short-term corrective measures in these areas that will, ultimately, allow the corrective process to take root. This applies, for example, to the need to introduce greater flexibility in the civil service so that a medium-term development process can begin.
- c. Governments cannot reform all sectors of the economy at once and it is often best to address different political constituencies in sequence (while maintaining the promise to pursue the whole Agenda in time). Thus, for example, the Federation (FBiH) government chose to tackle problems with pensions in the early stages and to defer potential layoffs in the public sector until later (when they could be properly planned and implemented).

For these reasons, it is useful to view the Reform Agenda as divided into three connected phases (as in Table 1):

- I. A first round of significant reforms was intended to demonstrate the commitment of the authorities to the reform process. It was a long list and, as a result, there were some delays. But all reforms were eventually concluded or introduced—as confirmed by the approval

of the new IMF and World Bank agreements. These included difficult political measures like: new Labor Laws in both entities; new collective agreements in both entities; sensible budgets at all levels, as well as some early privatization in the FBiH. Both entities introduced legislation to improve controls over spending—especially at social funds and at lower levels of government—and to strengthen the accountability of managers.

- II. A cooperative atmosphere was created during the first phase of reforms in 2016 that stimulated significant and impromptu plans to harmonize legislation across entities, particularly when it comes to fighting the gray economy and business regulation. As a result, the second phase began somewhat earlier than planned and included: the harmonization of Corporate Income Tax Laws between the entities, a new Bankruptcy Law in Republika Srpska (RS) that would be soon matched by a harmonized Law in the FBiH, the harmonization of laws on banks; and improved cooperation on banking supervision and bank resolution. Also, the FBiH government adopted a comprehensive set of pension reforms in 2016. The new FBiH Pension and Disability Law is now pending adoption by the FBiH Parliament and will be discussed as this book goes to print.
- III. Planning for the third phase of reforms in 2018 also began during 2016 and will continue during 2017. These plans will include meaningful restructuring in the public services at all levels (assisted by the World Bank), including long-overdue health reforms; the implementation of new Principles for PAR; the restructuring of SOEs, including railways and the large-scale liquidation of dormant enterprises in the FBiH (after resolving problems with unpaid social contributions for workers); and the privatization of some SOEs in the FBiH. These will be very difficult reforms—from a political perspective—but will (hopefully) benefit from momentum in the earlier phases.

### ***Support from the EU and International Financial Institutions***

The IFIs and EU were involved at all stages of the negotiation of the Reform Agenda and endorsed the final draft as a blueprint for the types of measures that could warrant medium-term financial support and other assistance. However, having learned the lessons from previous programs when structural reforms were never implemented, it was agreed that the authorities would need to demonstrate an early commitment to reforms, before any financial assistance was provided. As a result, the authorities

had to meet a long list of “prior actions” before the IMF’s EFF and World Bank’s DPL could be approved. In addition, the World Bank adopted an Employment Support Project in January 2017 and prepared separate programs that will support reforms in the health systems and in the railway sector (during later phases of the Reform Agenda).

Furthermore, the International Finance Corporation (IFC) is supporting the authorities in improving and harmonizing business legislation, as well as easier business registration. The United States Agency for International Development (USAID) completed work (ahead of time) on registers of para fiscal fees and the European Bank for Reconstruction and Development (EBRD) is providing assistance with the restructuring of SOEs in both entities (and could help finance a significant portfolio of infrastructure development).

To help defray the costs of reforms, the EU, IMF and World Bank plan to provide 800–850 million euros in direct budget support during 2016–2019. The IMF will provide 550 million euros while the World Bank and EU plan to provide some 150–160 million euros each. In addition, the World Bank and EBRD (and others) hope to facilitate or provide an additional 500 million euros in investment over three years. Private foreign investors will be also encouraged by reforms and the injection of these significant funds should help to boost growth and job creation.

## **Implementing the First Phase of Reforms and Planning for Later Phases**

This section provides a brief background on the need for reforms in each of the six categories of the Reform Agenda and briefly summarizes the progress achieved and upcoming measures.

### ***Public Finance, Taxation, and Fiscal Sustainability***

In its Report on BiH for 2015, the IMF identified three key fiscal weaknesses:<sup>7</sup>

- *An outsized public sector* with a high share of current spending. General government spending is among the largest in the region (see Chart 1a) and has the highest share of spending on wages and goods and services. The quality of public spending on health care and social

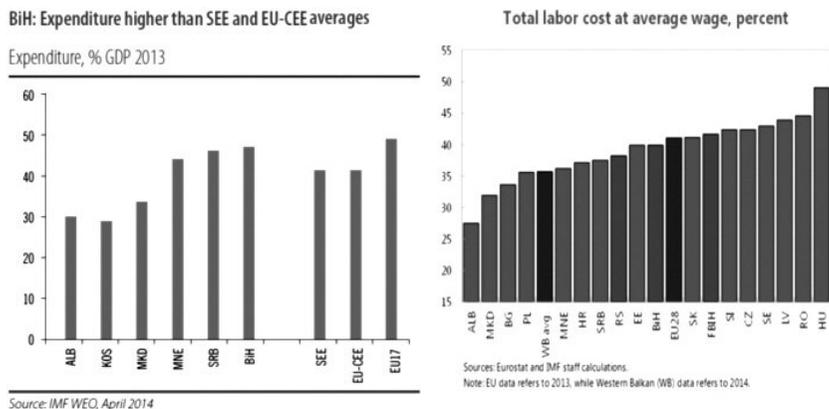
<sup>7</sup> IMF. 2015. *IMF Country Report No. 15/298*. p.12-13.

assistance is among the worst in the region, even though it is very high.

- *High tax burden on labor.* The tax wedge—comprising both personal income taxes and social security contributions—is relatively high in both entities compared to elsewhere in the region (Chart 1b). The high burden on labor is a strong disincentive for people to move from informal to formal employment or to enter the labor market.
- *Serious deficiencies in tax policy and revenue administration.* Revenues from corporate and personal income taxation are very low (even at high rates), mainly because of narrow tax bases. Generous incentives and low compliance erode revenues.

Particular progress has been made in:

- Adopting sound budgets in line with IMF recommendations for a second year in a row in 2017, including limits on hiring and a public-sector wage freeze. The authorities have committed themselves to reducing the overall government deficit to below 0.3 percent of GDP by 2018 with a view to reducing public debt gradually to below 40 percent of GDP over the medium term. Public debt is currently close to 45 percent of GDP.
- The four tax agencies combined all taxpayer information—as well as comprehensive company information from the entity business information agencies—into a database that is available and fully searchable in each of the four tax agencies.
- Both entities improved their revenue collection—by bolstering tax inspectorates and administrations—as witnessed by record levels of collection of indirect and direct tax revenues during 2016. In May of 2016, the Republika Srpska (RS) adopted a package of four laws to tackle the gray economy and there have been other combined measures by the entities to tackle the gray economy together.
- The World Bank has completed registries of arrears in the health sectors that will allow it to finalize concrete proposals for the reform of health sectors in both entities—to be supported by World Bank loans. The RS Government has already agreed with the World Bank on a comprehensive restructuring plan for the health sector to be launched in the second half of 2017.
- The FBiH government adopted new Laws on Personal Income Taxes and Contributions and a public debate about the need for tax reform is ready to begin in the fall of 2017. The laws will lower the employer's

**Figure 1. (a) Government Expenditure<sup>8</sup> and (b) Tax Wedge<sup>9</sup>**

tax burden (to promote the creation of new jobs), eliminate loopholes and make the calculation of salaries easier and more time efficient. Furthermore, the FBiH reduced contribution rates for low earners to a fixed amount. In December 2017, the RS undertook some initial steps towards lowering the tax burden on labour by eliminating the special solidarity contribution that was introduced following the 2014 floods.

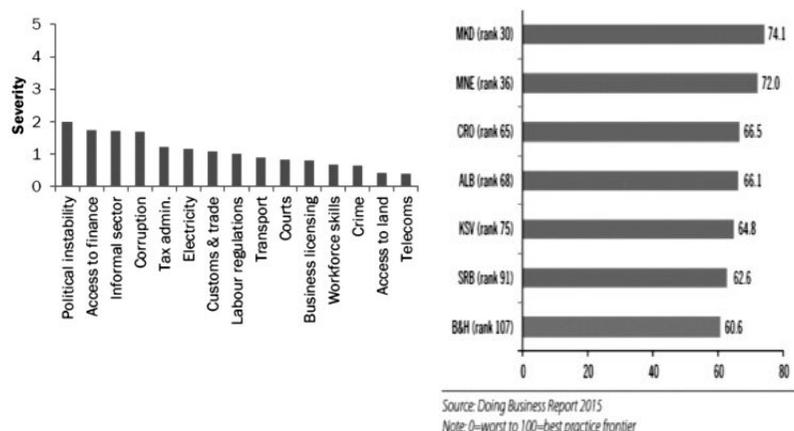
- In late 2016, the RS adopted a new Corporate Income Tax Law that is harmonized with the FBiH Law and in line with international best practices, to foster consistency and avoid double taxation between the entities.
- Both entities have strengthened controls over lower levels of government, extra-budgetary funds and SOEs and the BiH Council of Ministers and the RS adopted new Public Internal Financial Control Strategies.
- In April 2016, the BiH Council of Ministers adopted amendments to the Law on Borrowing, Debt and Guarantees, and proceeded to adopt BiH's first medium-term debt management strategy.

As of August 2017, the BiH Parliamentary Assembly has still not adopted the necessary legislation to raise fuel excises that are intended to generate

<sup>8</sup> World Bank Group. 2015. *Rebalancing Bosnia and Herzegovina—A Systematic Country Diagnostic*. p.42.

<sup>9</sup> IMF. 2016. *IMF Country Report No. 16/291*. p.8.

**Figure 2. (a) Obstacles to Doing Business<sup>10</sup> and (b) Regional Ranking<sup>11</sup>**



the resources necessary for the completion of the central motorway through the country. The legislation failed by one vote in April 2017 and has ever since been a victim of populism and political short-termism. This has caused delays with the IMF's EFF and, as a result, many other reforms are delayed as well. Moreover, the FBiH plans to provide loan or grant financing to cantons that restrain wages and reduce overall employment and it will amend its Law on Public Revenue Allocation to provide incentives for savings. In addition, the FBiH needs to amend its Law on Debt, Borrowing and Guarantees to improve financial control. Finally, the RS Government is expanding its treasury systems to the health sector to increase control.

### *The Business Climate and Competitiveness*

The business environment in BiH is the worst in South East Europe by many measures and needs major reform if the country is to boost private investment and improve competitiveness. The poor business climate requires entrepreneurs to overcome burdensome institutional and regulatory barriers that, ultimately, discourage new investment or expansion.

<sup>10</sup> EBRD. 2015. *Business Environment and Enterprise Performance Survey*. p.1.

<sup>11</sup> World Bank Group. 2015. *Rebalancing Bosnia and Herzegovina - A Systematic Country Diagnostic*. p.xiii.

Figure 2 sets out (a) the main obstacles to doing business (as reported in surveys) and (b) how BiH compares to other countries in the region. BiH suffers from perceptions of political instability, corruption and a lack of access to finance. The 2015 Doing Business report ranked BiH at 107<sup>th</sup> in the world and BiH is particularly bad when it comes to starting a business (147<sup>th</sup>), dealing with construction permits (182<sup>nd</sup>), paying taxes (151<sup>st</sup>) and getting electricity (163<sup>rd</sup>). These particular results indicate that starting a new business poses significant challenges.

In addition, firms are forced to spend a significant amount of time paying taxes and this can waste time and encourage tax evasion. Entrepreneurs face significant challenges from high social contributions, high fiscal and para-fiscal fees, restricted access to export markets, and a complicated and non-harmonized regulatory environment. Regional competitors like FYROM and Montenegro actively target improvements in these areas—to promote investment—and have had a good deal of success and higher growth that, in turn, gives momentum to further reform. Moreover, corporate governance is weak in BiH and offers insufficient protection to investors. Codes of corporate governance are not always implemented and there are significant differences between the existing corporate regimes in the entities.

The private sector's overall performance is stifled by the size of the public sector. Formal government expenditures are close to 50 percent of GDP but are likely to be far higher when SOEs are taken into account. This diverts resources—including labor, land and capital—away from the productive private sector. And, while the banking sector weathered the global financial crisis relatively well, non-performing loans increased and poor lending practices and a weak regulatory agency in the RS allowed serious problems to develop in two banks owned or connected to the government. In this context, credit to the private sector dried up and banks hold excess reserves at the Central Bank instead of lending to enterprises.

The Reform Agenda set out a comprehensive program to tackle these difficulties and particular progress has been made in:

- Improving the business environment: A new Law on Foreign Direct Investments was adopted at all three levels of government and the FBiH adopted a Law on Companies to create a more favorable business environment and attract foreign investors.
- The IFC and UK Embassy are supporting a project in Sarajevo Canton to tackle the longstanding issues of obtaining construction and

electricity permits (as noted above). Furthermore, Sarajevo Canton reduced costs and waiting times for business registration and recorded an increase of almost 20 percent in newly registered businesses. These measures should soon be mirrored in other cantons and the City of Banja Luka has just embarked on a similar project.

- USAID helped to complete registries of para-fiscal fees in all local governments and the RS adopted a law to codify them. The law (to be followed by a similar one in the FBiH) will increase transparency and tackle corruption by deeming as illegal any unregistered fees (that do not appear on the public online register). This will allow investors to plan ahead and should, in time, lead to reductions in administrative barriers and fees.
- A new Bankruptcy Law in the RS established a more efficient insolvency framework by introducing a process of “pre-liquidation” to allow financial restructuring while a business is still in operation (and allow the business to preserve jobs). A harmonized law has been adopted in the FBiH in first reading and is currently going through public debate.
- Both entities adopted new banking legislation and the State will amend the Law on Deposit Insurance to strengthen supervisors’ corrective and enforcement powers, introduce cross-entity supervision of banking groups, and introduce a comprehensive bank resolution framework. These strengthened banking structures should encourage bank lending to the private sector. In addition, two problem banks in the RS were liquidated and private depositors were compensated.
- The entities classified their SOEs and public companies into those that are strategic, those requiring minor or major restructuring, and companies in which the government holds a minority share. The governments will address the status of SOEs either through the restructuring and possible privatization of viable enterprises or the bankruptcy/liquidation of those that are not viable. The FBiH disposed of its minority stakes in two companies and most of the funds went to the rehabilitation of the pension fund in order to help ensure the regular payment of pensions. In 2017, the FBiH will contract reputable international advisors to conduct the financial and operational due diligence of BH Telecom and HT Mostar with the objective of restructuring and/or selling of shares.

- The World Bank presented its analysis on options for railways in both entities at the end of 2016 and the RS Government, in agreement with the unions, has already undertaken the first steps to restructure the entire sector. The FBiH is still considering options
- A new Law on Customs Policy entered into force in August of 2015 simplifying customs processing procedures and reducing administrative requirements. Activities on continuing the inspections reform and strengthening national quality control in line with EU requirements are well advanced.
- The World Bank presented a Feasibility Study for Establishing Commercial Courts in the FBiH in late 2016 and recommended that existing commercial case departments be reorganized and strengthened rather than establish new courts (as initially envisaged under the Reform Agenda). The RS will strengthen its commercial courts.
- In cooperation with the IFC, the FBiH has made significant progress toward establishing “one-stop shops” for business registration—in line with systems already in place in the RS—and both entities will simplify and establish joint online registration procedures by the summer 2017.

### *The Labor Market*

The labor market in BiH is characterized by notably worse outcomes than in most other countries in emerging Europe, including many countries in the Western Balkans. In 2013, the unemployment rate stood at 27.5 percent according to the annual Labor Force Survey conducted by the BiH Agency for Statistics.<sup>12</sup> This situation was further complicated by a high rate of long-term unemployment and a youth unemployment rate of around 60 percent—the worst in the region (see Chart 3a). Surveys revealed that restrictive labor regulations are regarded as a major constraint to employment (see Chart 3b).

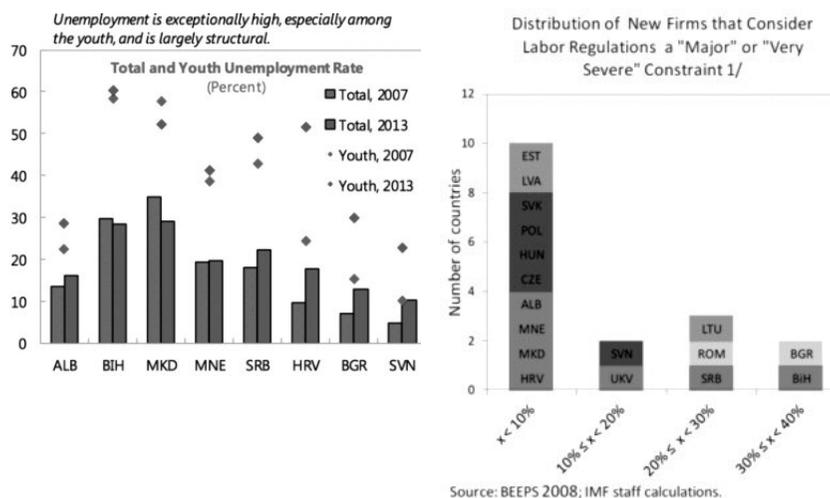
More generally, private sector employment creation was hampered by: high administrative barriers for employees; the need to grant extensive benefits; complicated and inconsistent laws that are not harmonized across jurisdictions; and different interpretations of labor relations by the courts that create uncertainty for both employers and employees.<sup>13,14</sup> Further-

<sup>12</sup> BiH Agency for Statistics. 2013. *Labor Force Survey 2013*.

<sup>13</sup> South East Europe Legal Group. 2011. *Employment Guide 2011*.

<sup>14</sup> Foreign Investors Council. 2013. *White Book 2012/13*.

**Figure 3. (a) Total and Youth Unemployment Rates<sup>15</sup> and (b) Labor Regulations<sup>16</sup>**



more, the high costs of starting to work were matched by high costs of terminating employment that included the requirement to continue to pay social contributions while a business is in liquidation. Difficulties in terminating employment severely discourage employers from hiring workers in the first place. Employers need to have a measure of flexibility before they will employ an expensive workforce that is subject to high taxes and influenced by high wages in the public sector.

In these circumstances, many people have given up on the prospect of finding work and, as a result, BiH has the lowest rate of labor market participation (or “activity”) in Europe at just 43.6 percent.<sup>17</sup> According to World Bank calculations, there are too few people with formal private sector jobs—too few to sustain a country aspiring to become an EU member.

Young people, because they have little employment history, are at a particular disadvantage. And because they are often willing to accept temporary arrangements in order to get a start in life, they are even more damaged and discouraged by restrictive hiring practices, a lack of flexibility in col-

<sup>15</sup> IMF. 2016. *IMF Country Report No. 16/291*. p.6.

<sup>16</sup> IMF. 2016. *IMF Country Report No. 15/299*. p.23.

<sup>17</sup> See IMF Working Paper. 2014. *Boosting Job Growth in the Western Balkans*. p. 5 for the European comparison and BiH Agency for Statistics. 2013. *Labor Force Survey 2013* for the data.

lective agreements (between employers and unions) and barriers to temporary work. They are often driven into a gray market that offers little or no training.<sup>18</sup>

The Reform Agenda set out three sets of measures to improve the labor market and particular progress has been made in:

- Making the labor market more flexible by introducing new and harmonized labor laws in both entities that: (i) impose term limits on the duration of collective agreements and mandated the renegotiation of existing agreements; (ii) allow wages to be better linked to performance; (iii) reduce disincentives for hiring by increasing opportunities for part-time work and fixed-term contracts and by limiting severance payments to no more than six months of wages; (iv) better protect workers' rights and reduce informal employment by increasing penalties for labor code violations; and (v) in the RS, eliminate a take-home pay protection. These new laws are supported by stepped-up labor inspections and increased penalties for violations to protect workers' rights that are consistent with ILO labor standards and EU labor directives.
- A new General Collective Agreement in the FBiH entered into force in July 2016, and the FBiH had completed negotiations on 24 out of 29 new branch collective agreements as of early 2017. The RS completed negotiations on its new General Collective Agreement in January 2017.
- The World Bank approved an Employment Support Project in February 2017 that will streamline active labor market policies, strengthen employment bureaus and provide modern retraining. It aims to separate the administration of health insurance from the role that employment bureaus play in mediating employment and allow them to concentrate on the latter role. Also, in order to increase labor market participation, both entities have introduced support schemes for first-time job seekers and the self-employed.

---

<sup>18</sup> There is a general perception that access to a first job depends on being on the "inside" and surveys list corruption and nepotism as the main barriers to youth employment (see Pavelic, D. 2007. *Study on Youth Employment in Bosnia and Herzegovina*. p.43). Young people aged 15-24—who make up one tenth of BiH's population—are the most vulnerable group on the labor market. In 2013, young people presented only 5.9% of BiH's overall employment, while the unemployment rate was more than twice as high compared to the rest of the population (see Friedrich Ebert Stiftung. 2014. *Youth Study Bosnia and Herzegovina*. p.63). By comparison, in the European Union a third of young people had a job in 2013 (see European Commission. 2014. *EU Employment and Social Situation, Quarterly Review*. p.5).

- Finally, in order to better link the education system to the demands of the labor market, the RS adopted a Development Education Strategy for 2016–2021, as well as a Strategy for Scientific Research and Technology Development for 2017–2020.

### ***Social Welfare and Pension Reform***

In addition to promoting initiative and industry, a modern caring society must provide for those that cannot take care of themselves. There are two broad categories of social assistance in BiH: insurance-based benefits that are funded by contributions from workers—especially for pensions; and (non-insurance) cash transfers from the budget to some members of the general population. The first category is supposed to fund itself and the second category is intended to make transfers to those people who are most in need of help. Both systems are severely out of balance.<sup>19</sup>

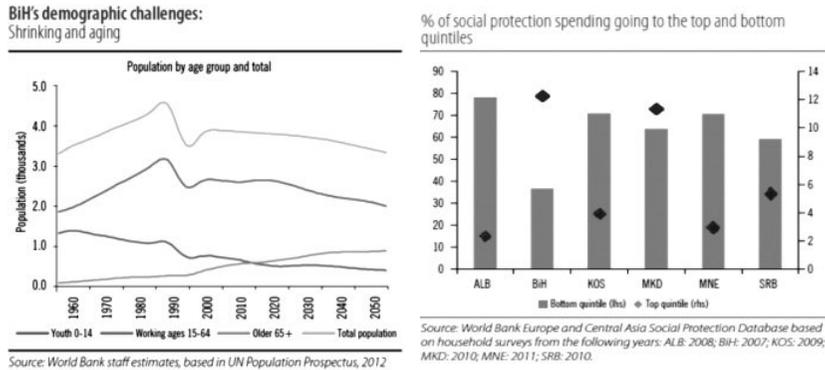
BiH spends twice as much on non-insurance cash transfers as the average in transition economies. On the whole, the social welfare system is not financially stable. And, most importantly, the dynamics and incentives are toward further deterioration in the funding base and an increase in costs. World Bank studies have concluded that a complete makeover is needed, if the system is not to implode:<sup>20</sup>

- Pension systems already have a small contribution base because of the low percentage of employed people and also have to contend with an aging population and significant emigration of the young. In 2014, for the first time, the country had more old people (over 65 years of age) than young people (see Chart 4a). As in other aging European countries this poses significant challenges for the sustainability of pension systems.
- Despite a large share of GDP used for social security and other social benefits, these benefits fail to adequately reach the poor. Only 37 percent of benefits are received by the poorest 20 percent (Chart 4b) and, at the same time, over 12 percent of public spending on social benefits reaches the wealthiest 20 percent of the population. This is significantly worse than any other country in region. At the

---

<sup>19</sup> World Bank Group. 2015. *Rebalancing Bosnia and Herzegovina—A Systematic Country Diagnostic*. pp. 79–81.

<sup>20</sup> World Bank Group. 2012. *Bosnia and Herzegovina—Challenges and Directions for Reform: A Public Expenditure and Institutional Review*.

**Figure 4. (a) Age Profiles<sup>21</sup> and (b) Social Protection in BiH<sup>22</sup>**

same time, only 30 percent of the people of BiH are satisfied with the benefits that are available.

In addition to these problems:

- A comprehensive strategy is needed to tackle the issue of unpaid social security contributions by SOEs. Some 65,000 employees are still on the payroll of a large number of SOEs that no longer operate effectively but continue to build up arrears in unpaid social contributions. The SOEs cannot be closed without agreeing a settlement with workers for missing benefits and the employees do not want to move on to other employment for fear of losing their rights.
- BiH was the only country in the region that has not set regulations for voluntary pension funds. This deprives people of a safe and liquid depository for their individual pension savings and further diminishes the prospects for resolving the aging problem in BiH.

The Reform Agenda includes measures to: (a) ensure sustainability of the pension systems; (b) improve the efficiency of social welfare support, primarily through better targeting of social assistance to protect the most vulnerable while containing the costs of benefits to others by completing audits of beneficiaries; (c) clear arrears in social funds in the FBiH; and (d) introduce voluntary pension funds.

<sup>21</sup> World Bank Group. 2015. *Rebalancing Bosnia and Herzegovina—A Systematic Country Diagnostic*. p.viii.

<sup>22</sup> Ibid. p.81

Particular progress has been made in:

- Improving pension sustainability: The FBiH government adopted a pension reform package consisting of Laws on Pension and Disability Insurance and on the Organization of the Pension and Disability Insurance Fund that will hopefully be adopted in the fall of 2017. These Laws will help ensure the sustainability of the pension system by, *inter alia*, raising the retirement age, increasing the number of contributors and broadening the contribution base. The RS undertook significant reforms of its social welfare and pensions system in 2011–2012 and the measures now achieved in both entities will have a very positive fiscal and social impact. However, a second round of parametric reforms could be needed over the medium term.
- In addition, the first Voluntary Pension Fund will start its operation in the RS by the end of 2017 and the FBiH is preparing the necessary legislation to establish similar funds.
- An audit process to verify the eligibility of war veterans for benefits (including privileged pensions) should go through its final stage by the end of 2017. In addition, in order to improve the targeting of social benefits, the FBiH must prepare a plan to improve the targeting of social transfers based on a centralized database of beneficiaries that is about to be established.
- The FBiH Government has prepared lists of eligible workers, projected the relevant liabilities and plans to set aside some BAM 450 million over 11–12 years to make up for unpaid contributions for the aforementioned workers from SOEs. The payments will allow these workers to retire with full benefits and the mostly-dormant enterprises will then be closed. This major clean-up exercise will be finalized with the adoption of a Law on Missing Pension Contributions that is under preparation and should be discussed in the following months.

## **Rule of Law and Good Governance**

Corruption retards development and growth and leads to the inefficient implementation of public policies. It results in a waste of public expenditure and a significant loss of tax revenue. More generally, it leads to an ineffective distribution of the talent and resources available to the economy. Incumbents benefit at the expense of others and any social consensus behind reform is undermined. A lack of trust in law enforcement and the judiciary

is detrimental both to citizens and to investors. Adherence to the rule of law and good governance is crucial to the accession process and is a precondition for economic and social development.

Corruption kills initiative and investment in any economy and potential investors often rely on surveys (like the *Corruption Perceptions Index* compiled by Transparency International) to tell them where they should not invest. BiH sits on the top rung of republics of the former Yugoslavia when it comes to perceptions of corruption and was ranked 72<sup>nd</sup> out of the 175 countries surveyed in the world (see Figure 5a) in 2013. According to other surveys, almost three quarters of business people in BiH view corruption as a significant obstacle to doing business and a significant proportion decide against investing due to fears of bribery. More broadly, corruption is ranked as the third most important obstacle to investment in the region.<sup>23</sup> And connections are regarded as being particularly important in BiH (Figure 5b)

Strategies for combating corruption, associated Action Plans, and bodies monitoring these practices are needed. Some improvements over the past few years—like the passage of Laws on Public Procurement and Whistleblowing—must be supported by stronger implementation and collaborative law-enforcement measures; notably with regards to information exchange. More generally, economic corruption will continue to thrive in an environment of complicated and semi-hidden rules and regulations and uncertainty over procedures for the issuance of licenses and permits. Therefore, there is a need for greater clarity, simplicity and transparency in administrative procedures and fees—like the aforementioned public listing of para-fiscal fees and other costs.

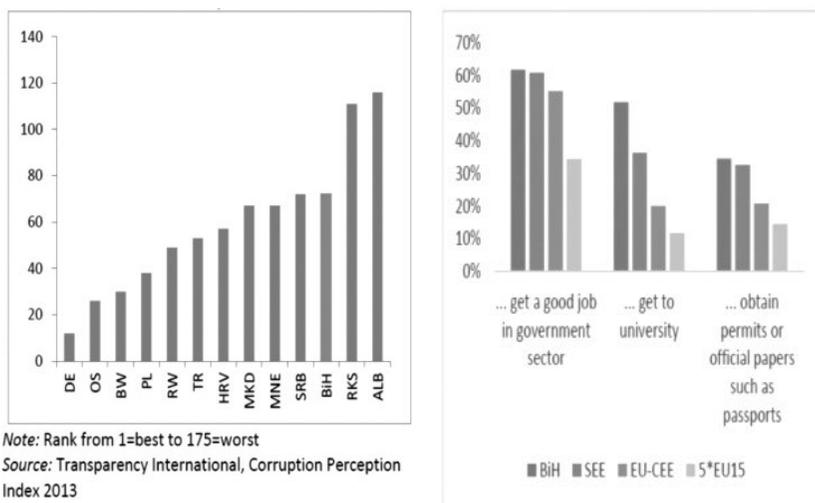
The State Institutions need to take a leading role in development of the Rule of Law and the High Judicial and Prosecutorial Council (HJPC) is the state institution that oversees the entire judiciary in BiH. Common principles need to be agreed in areas such as personal data protection, civilian possession of weapons and asset declaration.

The Reform Agenda set out an extensive list of measures to improve the rule of law and notable progress has been made in adopting a number of strategies and action plans in an effort to strengthen the judiciary and combat corruption, organized crime and terrorism. The years 2017–2018 will be dedicated to the implementation of the following:

---

<sup>23</sup> UNODC. 2013. *Business, Corruption and Crime in the Western Balkans: The Impact of Bribery and Other Crime on Private Enterprise*. p.46.

**Figure 5. (a) Transparency Ranking<sup>24</sup> and (b) Percentage that believes connections are “Very Important in order to ...”<sup>25</sup>**



Note: Rank from 1=best to 175=worst  
 Source: Transparency International, Corruption Perception Index 2013

Source: LITS, 2011 and staff calculations

- A Justice Sector Reform Strategy was adopted in September 2015 and aimed at ensuring a harmonized and coordinated reform of the judiciary involving all levels of authority in BiH. This was followed by a major breakthrough with the adoption of the Justice Sector Reform Strategy Action Plan in March 2017.
- In July 2016, the HJPC adopted a number of operational guidelines to be followed by Courts and Prosecutor’s Offices throughout BiH and which are aimed at fulfilling the Reform Agenda requirements on strengthening disciplinary sanctions, combating conflict of interest in the judiciary and improving integrity.
- Concerning law enforcement, legislation was adopted to secure a greater level of financial and operational independence in the conduct of police operations (thus reducing the risk of undue political influence). As regards police cooperation, an Agreement on Mutual Assistance and Operational Cooperation was signed between the State Investigation and Protection Agency (SIPA) and the relevant bodies

<sup>24</sup> World Bank Group. 2015. *Rebalancing Bosnia and Herzegovina—A Systematic Country Diagnostic*. p.9.

<sup>25</sup> *Ibid.* p.10.

in the RS, FBiH and Brčko District in December of 2015. In addition, an Agreement on Operational and Strategic Cooperation between BiH and Europol was ratified by the BiH Presidency in March 2017.

- Strategies for combating corruption and associated Action Plans were adopted at State and entity levels and dedicated bodies are now in place at entity and state level. Structures for the prevention of corruption have been or are being established at all levels of authority and policy documents are in place or pending.
- The Integrated Border Management (IBM) Strategy and Framework Action Plan of BiH for 2015–2018 entered into force on January 1<sup>st</sup> 2016. This determines the further development of a Joint Risk Analysis Centre and establishes a risk analysis concept for BiH in general terms. However, the IBM Strategy and Action Plan require further development of the Joint Centre for Police Cooperation (in Trebinje) and additional support for the overall improvement of security policy through a more efficient fight against all forms of cross-border movement and organized crime.
- Finally, an Action Plan for implementation of the BiH Counterterrorism Strategy was adopted by the BiH Council of Ministers in October 2016.

## Public Administration Reform (PAR)

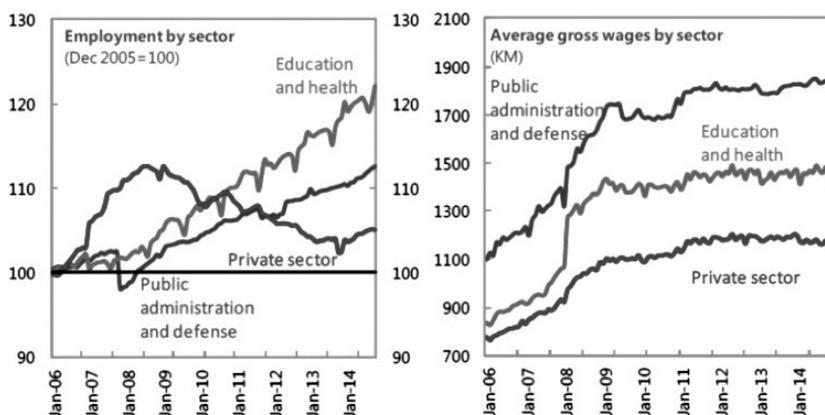
The public sector controls well over half of the economy of BiH, with direct expenditures at close to half of GDP and SOEs adding even more quasi-government control. According to the World Bank, BiH has one of the largest public sectors in the world. This state dominance retards economic growth and employment and undermines prospects for the poor and other excluded groups—like younger people. Much of public expenditure is inefficient and fails to reach the people or investment areas that most need it. Moreover, the current situation breeds opportunities for poor governance, including corruption and nepotism. And, while BiH has the largest public sector wage bill in the region, its citizens do not enjoy a correspondingly high quality of public services.<sup>26</sup>

The public sector crowds out potential private-sector activity and the situation is—if anything—getting progressively worse. Chart 6 demon-

---

<sup>26</sup> World Bank Group. 2015. *Rebalancing Bosnia and Herzegovina - A Systematic Country Diagnostic*. p.33.

**Figure 6. Public Sector Growth<sup>27</sup>**



Source: BIH Agency for statistics, and IMF staff calculations.

1/ Private sector employment includes workers employed by a number of state-owned enterprises.

strates (a) how public-sector employment rose at the expense of private-sector employment in 2006–2014 and (b) how gross wages in the public sector exceed private-sector wages by increasing margins. Clearly, the economy had come to a tipping point in 2014 that could see the private sector shrivel further.

The Reform Agenda recognized an urgent need for significant public administration reform in order to ensure fiscal sustainability and the improved quality of public service delivery to citizens. It expressed a clear need to reduce the size of the government sector in the economy and to significantly lower the tax burden on work and investment. These imperatives point to the need to significantly reduce public expenditure at all levels of government and to improve its efficiency. The Reform Agenda promised, at the same time, to strengthen administrative capabilities and increase efficiency in public institutions at all levels of government.

The following progress was made in:

- Placing limits on hiring and wages: Temporary restrictions on wage and employment increases in the public sector were put in place in the Laws on Budgets for 2016 and 2017 by both state-level institutions and entities and there are already signs of shrinkage in public

<sup>27</sup> IMF. 2016. *IMF Country Report No. 15/299*. p.21.

sector employment. These restrictions will remain in place until detailed strategic plans for improved wage setting mechanisms and significant cuts in employment have been agreed with the World Bank and a methodology has been put in place to put salaries in the public sector on a sustainable basis.

- **Public sector rightsizing:** The World Bank is assisting (with the support of the EU) the state institutions and entities to complete the first-ever complete registries of public employment at all levels of government in BiH and these should serve as the basis for operationalizing the strategic plans on reducing public sector employment that will be required by the IMF in 2018 (under the terms of the EFF).
- In late May 2017, the RS parliament plans to adopt a Public Financial Management Strategy that will match strategies already developed by the state institutions, FBiH and Brcko District. After a period of consultation and consolidation, a country-wide PFM strategy will be prepared. The Strategy will significantly improve the planning and coordination of fiscal policies across entities and state institutions and permit greater transparency and control in government expenditure. The strategy will also allow the EU to provide budget support to other sectors—such as energy or transport—in support of the Reform Agenda.
- **Publishing the census results:** The results of the population and housing census conducted in October 2013 were published in June of 2016 and will permit improvements in socioeconomic planning at the local level. The census was conducted in compliance with international standards, according to the International Monitoring Operation, and is the first census to be concluded since the war.
- **Adopting key principles of PAR:** An Operational Plan for the elaboration of a new PAR Strategic Framework was prepared in December 2015 with the support of the EU. It presents the key issues for strategic development, including working structures and a timeframe. And, in February 2017 the first PAR Special Group meeting between the EU and local authorities took place in Mostar. This has started the process for all levels of government to adopt a country-wide PAR Strategic Framework.
- All three governments drafted amendments to their Laws on Civil Service in order to comply with new Labor Laws. The FBiH adopted changes that place term limits on senior management positions and

launched competitions to refill these positions by mid-2016 according to clear criteria. The EU objected that the selection process could become too political but the FBiH Government sees their approach as a stop-gap measure—to demonstrate that all senior managers can be replaced and that none of them have permanent positions—until more-permanent institutions and structures can be established.

- Ensuring transparency in procurement and hiring: An electronic system for publication of decisions of the Procurement Review Body has been put in place.<sup>28</sup> The 2015 decisions of the Procurement Review Body were published in the portal, although no upload for the years before 2015 have yet been made.

## **Conclusion: Planning and Monitoring of Further Reforms**

On September 20, 2016, the General Affairs Council (GAC) of the EU welcomed “meaningful progress in the implementation of the Reform Agenda” and invited the European Commission to submit its opinion on the country’s membership application (that was submitted on February 15, 2016). Thus, thanks in part to progress under the Reform Agenda, BiH was back on its EU accession track after a hiatus of eight years from the initial signing of a Stabilization and Association Agreement (SAA) in 2008. At the same time, the GAC called on BiH to “continue its efforts to ensure effective implementation of the Reform Agenda [...] in close cooperation with the European Union, international financial institutions and international partners, as well as civil society.” There has been a greater sense of momentum behind socio-economic reforms than has ever before been achieved in BiH.

The approval of substantial programs with the IMF and World Bank also marks a very important milestone in the implementation of the socioeconomic aspects of the Reform Agenda. Both programs are designed to combat deep-rooted structural problems in the economy over a three-year period and are closely coordinated in support of the Reform Agenda. The IMF has, in this context, noted that the Reform Agenda “[...] promises perhaps the most significant reorientation of the BiH economy since the time of the Dayton Accords. The Agenda builds on the lessons learnt from earlier performance, namely the need to reform labor laws and improve the compo-

---

<sup>28</sup> Available at [www.ejn.gov.ba](http://www.ejn.gov.ba).

sition of government spending. It also emphasizes the need to harmonize rules and regulations and to improve intra-governmental coordination.”<sup>29</sup>

These flagship programs will together guide the implementation of deep-rooted and long-overdue structural reforms over the next period. And they will continue to be strongly supported by complementary programs and assistance from the EU, the EBRD, USAID, the IFC and others. A lot of detailed work still needs to be completed and implemented on issues such as SOE restructuring, public employment restructuring, PAR, health sector reform and the implementation of strategies to enhance the rule of law. These reforms require strong political commitment and, given the fact that BiH enters another general elections cycle in 2018, it will unfortunately become increasingly difficult to pursue their implementation.

As regards to the monitoring of the Reform Agenda, the authorities have themselves initiated the production of quarterly Progress Reports, complete with detailed Action Plans across state institutions and entities that identify the institutions responsible for each measure, the progress made, and deadlines for completion. The March 2017 Action Plan, for example, listed around 200 measures and sub-measures that needed to be completed (or that were completed) in support of the overall Agenda. This makes the point that reforms are complicated and need to be implemented and supported by the authorities themselves—the people who know how the system operates in detail and how it needs to be changed.

Of course, it is also essential to have external encouragement and assistance, and the international community has compiled an impressive package of financial incentives and technical assistance. Progress is closely monitored according to strict conditions for the release of assistance. The IMF, in particular, will conduct quarterly reviews of performance against pre-agreed benchmarks across a whole range of issues and the disbursement of financial assistance will depend on satisfying these benchmarks. These benchmarks will guide and encourage the authorities to remain on track with the implementation schedule. The EU and World Bank have established their own conditions for disbursing financial assistance.

The Reform Agenda survived many political squalls in BiH during the second half of 2015, through the whole of 2016 and into 2017. It has—in addition to being a focus for reforms—served as a focal point for political cooperation and the pursuit of compromise. This political process—where

---

<sup>29</sup> IMF. 2016. *IMF Country Report No. 16/291*. p.5.

institutions learn to adapt to one another in practical ways—is almost as important as the pursuit of reforms itself. And, sometimes, there are delays. The approval of the IMF program was delayed because of an extensive set of prior actions, for example, and there is currently a delay in approving the first review of the arrangement. But the IMF has promised to persevere and to be understanding and recognizes that significant achievements have already been made. The Reform Agenda has, therefore, succeeded in providing a framework to overcome temporary difficulties and has delivered sufficient momentum to encourage both the authorities and the EU and IFIs to persevere in the face of inevitable challenges.

Altogether, the commitment of the authorities to an Agenda that was generated in consultation with civil society and negotiated in detail across all levels of government is being strongly supported by a closely-coordinated international community. All of the necessary structures and processes are in place. But, it will take more time for the benefits of reforms to become clear to the general public and this is the last and crucial requirement for success.

So, the reform process is now at a critical juncture: reforms have begun in earnest and there have been significant political costs for governments; but broad-based political support for credible change has not yet materialized. There is an inevitable gap in confidence on all sides.

The international community has stepped into this breach with financial support for budgets and political support for a renewed EU accession process. This is intended to push the reform process into its final stages. But it remains to be seen whether this support will be enough to encourage the authorities—as brave as they have been—to stay on course until positive results become clear. This is a very important time for the people of BiH.



## *Chapter 2*

# **Bosnia and Herzegovina: Reform Agenda and the Effects of its Early Implementation Phase**

*Goran Mirašćić*

Bosnia and Herzegovina (BiH) has accomplished a great deal since experiencing a war in the 1990s. Today, BiH is a potential European Union (EU) candidate country moving toward alignment with the EU's *acquis* requirements. Between 1998 and 2008, BiH experienced strong growth, with the gross domestic product (GDP) increasing by over two-thirds in real terms, and poverty dropping from nearly 20 percent to around 14 percent during the same period.<sup>1</sup>

Despite this strong economic performance, the onset of the global financial crisis in the fall of 2008 is having an enduring negative impact on the country's economy. The economy rebounded in 2011—growing by one percent after a deep recession in 2009 caused GDP to contract by 2.9 percent—before returning to a recession in 2012.<sup>2</sup> In 2013, the economy grew by an estimated 0.8 percent, mostly due to increased exports. The World Bank forecasted a continued rebound in 2014, with an estimated growth rate of 2 percent. In 2015, the country marked a 3.2 percent growth rate in real GDP terms, with an intention for the growth to reach 4 percent by the end of 2016, and 4.4 percent in 2017.<sup>3</sup>

Despite this relatively positive outlook, risks continue to tilt economic growth downward. In particular, slower growth in the main Eurozone export markets, domestic political and social turmoil, lack of progress in making improvements in the business climate (through streamlined regulations, trade procedures or lack of progress on transport links) could all reduce the economic growth rate indicators.

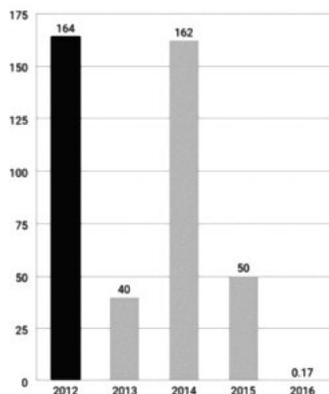
The country needs to achieve significant progress in implementing structural reforms if it is to achieve faster economic growth than what is currently foreseen. Strengthening public finance, improving the business

---

<sup>1</sup> The World Bank, <http://www.worldbank.org/en/country/bosniaandherzegovina/overview>.

<sup>2</sup> Central Bank of Bosnia and Herzegovina, [www.cbbh.ba](http://www.cbbh.ba).

<sup>3</sup> BiH Directorate for Economic Planning, [www.dep.gov.ba](http://www.dep.gov.ba).

**LENDING****Bosnia and Herzegovina: Commitments by Fiscal Year (in millions of dollars)\***

\*Amounts include IBRD and IDA commitments

**Bosnia and Herzegovina****Country At A Glance**

Population	3,791 million	2015
GDP	\$ 16,00 billion	2015
GDP growth	3,20 percent	2015
Inflation	-1,00 percent	2015

environment in the country, and advancing the institutional and labor market reform agenda are among the areas where Bosnia and Herzegovina could make notable progress in fostering job creation and growth in the medium term.

### Why Should BiH Undergo Intensive Economic Reforms?

There is an opportunity to reform the business environment and to make the tax system and public finances more sustainable. The size and role of the government sector must be reduced. The public sector is far too expensive for a country the size of Bosnia and Herzegovina. This is not simply because of the complex and multi-layered Dayton structures, it is also the result of decades of political cronyism. A serious public administration reform will, moreover, increase the confidence of investors and, hopefully, get domestic banks to start lending again on a significant level. Make no mistake: BiH does not suffer from a liquidity problem. Rather, banks hold more money at the Central Bank than is required of them, simply because they cannot find adequate projects to finance. Investors and company leaders need to see a brighter future through the fog of government regulation and taxes before they are willing to hire new employees. Bosnia and Herzegovina lacks monetary independence, as the Central bank is currently operating under the Currency board arrangement. The only instrument the Central Bank has at its disposal is prescribing the

minimum level of reserves commercial banks are required to keep. As of July 1, 2016, the Central Bank has amended its policy, which now states that the Central bank will pay interest rates on above-reserves kept by commercial banks in the amount of 50 percent of the ECB interest rate. Basically, this means that the interest rate is regressive so that commercial banks are stimulated to revive their lending. A freeze on wages and on the hiring of new employees in the public sector will also send a strong signal to voters that it is not merely the general population who are expected to change their behavior but institutions as well.

New labor laws and practices are crucial elements in improving the business environment, as all of the relevant domestic and international actors working with BiH identified this particular area as one of the biggest barriers to increasing the overall investment level. Flexibility in the labor market must be increased and consequently, opportunities for finding decent employment—especially for young people—would improve tremendously. Equal access to employment opportunities is a fundamental economic and social right enshrined in many international conventions. The new labor laws intend to make employment secure and fair, rather than exclusive. The Labor Law adopted by the Federation of Bosnia and Herzegovina (FBiH) government and parliament in July 2015 includes 26 articles on strengthening the rights of workers, for example through generous maternity and paternity benefits, making it more in line with European standards than the previous law. In addition, the new law allows employers and employees to adapt to changing circumstances, which is particularly important when promoting increased investment. The objective of each labor-related legislation is to establish a flexible market that can easily adapt to a changing economic environment.

Business-related reforms need to go hand in hand with the further entrenchment of the rule of law and good governance principles. Criminal investigations must be expeditious, efficient and thorough, while sanctions should be a deterrent and actually enforceable. A corrupt-free business environment supported by an accountable, professional and efficient judiciary is an essential pre-condition to restore citizens' confidence and foreign investors' trust.

Reforms will be difficult to implement, but they will ultimately benefit society as a whole. BiH has to establish a system where social benefits like pensions and healthcare can be secured for those who are most in need. Vulnerable people, the elderly, disabled, and those who suffer scars from one of the worst conflicts Europe has seen since World War II need to

receive decent support. This is to be achieved through better targeting, meaning that assistance should be provided to those in need. It is an illusion that BiH can spend more on social affairs, as it, on average, already spends more than other countries in the region. Short-term improvements can come from better targeting practices through an audit process that excludes false users.

At the same time, opportunities for people who are ready and able to work need to be created, as too many have already left the country or are considering doing so if no improvement is in sight. BiH needs to get to a situation where the government is seen as a help rather than a hindrance, and most of all, where people can look forward to a fruitful life in their own country.

## **The British-German Initiative**

### ***Need for Implementation of Social Reform, Strengthening of the Economy, and Job Creation***

On the heels of the October 2014 general elections, representatives of Germany and the United Kingdom announced a new initiative to engage with Bosnia and Herzegovina and re-shape its European integration path after years of stalemate or even regression. The initiative included all of the off-the-shelf ingredients of previous efforts to jump-start the reform process in BiH, such as written commitments (applied in the past to police reform, constitutional reform, etc.) and a reform agenda (as in the Partnership Document).

## **Compact for Growth and Jobs**

The Reform Agenda is a result of the most extensive consultation process BiH has ever seen. It is firmly based on the economic-social programs of all governments in the country; that is, the Council of Ministers, FBiH, Republika Srpska (RS), the Brcko District, and all ten cantonal governments. The “Forum for Prosperity and Jobs” in May 2014, attended by a spectrum of civil, academic, business and political society, provided initial inspiration. Further inputs were received at expert and public events, including at local gatherings with citizens throughout the country, as well as online platforms. In short, this process included all of the relevant domestic and international stakeholders.

## **Reform Agenda Political and Economic Context-Process of Recovery**

The adoption of the Reform Agenda<sup>4</sup> by Bosnia and Herzegovina authorities is a crucial step forward for the country's EU integration path. In July 2015, both entity governments and the Council of Ministers adopted a Reform Agenda for the period 2015–18 for Bosnia and Herzegovina. This particular document outlines the main sectors that require reforms, which has been established with the assistance of the EU Delegation to BiH, and in cooperation with international financial institutions. While the people of BiH have issues on which they repeatedly fail to achieve consensus, the Reform Agenda is something they all agree on. One could even go as far as to say that this is the most significant document endorsed by all groups.

The document comprises six key sectors, later developed into a single action plan, outlining specific activities and the institutional responsibility for each:

1. Public finance, taxation and fiscal sustainability;
2. The business climate and competitiveness;
3. The labor market;
4. Social welfare and pension reform;
5. Rule of law and good governance;
6. Public administration reform

Reform Agenda priorities by years:

2015: Labor legislation, preventing the growth of public expenditure for civil servants, support of employment;

2016: Business environment, commercial courts, registration, licenses and also employment support;

2017: Public-private partnership, concessions, exploitation of resources, attracting investment.

---

<sup>4</sup> Reform Agenda for Bosnia and Herzegovina 2015–2018; <http://europa.ba/wp-content/uploads/2015/09/Reform-Agenda-BiH.pdf>.

### **Achieved Milestones:**

The consent of the Federal Government for implementation - September 17, 2015

The Action Plan agreed with the Government of the RS - September 9, 2015

The Action Plan contains 61 activity / period of implementation (three years)

Treats six areas of Reform Agenda

Eighteen activities fully accomplished by August 2016

### **Federation of Bosnia and Herzegovina: Summary of Macro-Indicators 2015/2016**

#### Snapshots of Macroeconomic Indicators

- Net increase in number of employees 23,178; (Tax Administration Office, for the period March 31, 2015 to July 31, 2016)
- Growth of indirect tax revenues of 3.5 percent; (Tax Administration Office FBiH, for the period March 31, 2015 to July 31, 2016)
- Growth of real GDP of 3.16 percent, with the intention that the growth reaches 4 percent by the end of 2016. (4.4 percent in 2017)<sup>5</sup>
- Growth of direct tax revenues for the first eight months of 2016 rose by 10.32 percent compared to the same period a year before<sup>6</sup>

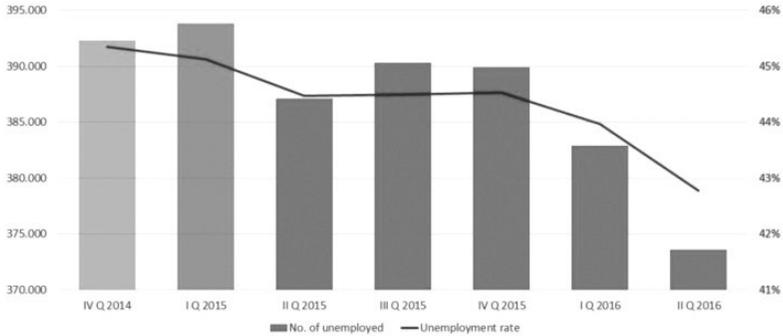
In short, the FBiH government has fulfilled 28 percent of the activities envisaged by the Reform Agenda Action Plan. These macro-indicators are not spectacular, but they prove that the negative trends have been stopped, and that better days are ahead. We can, with certainty, state that these positive indicators come as a result of economic measures undertaken by the FBiH government, and that the economy has positively responded. Unfortunately, this GDP growth is mainly the result of internal (push) forces, as regional (pull) forces are not strong enough to carry the weight of reform. Comparatively, growth in BiH is higher than its neighboring countries in the region with the exception of Macedonia, which reported growth of 3.5 percent. The prospects for regional economic growth remain

---

<sup>5</sup> Statistics Agency of FBiH.

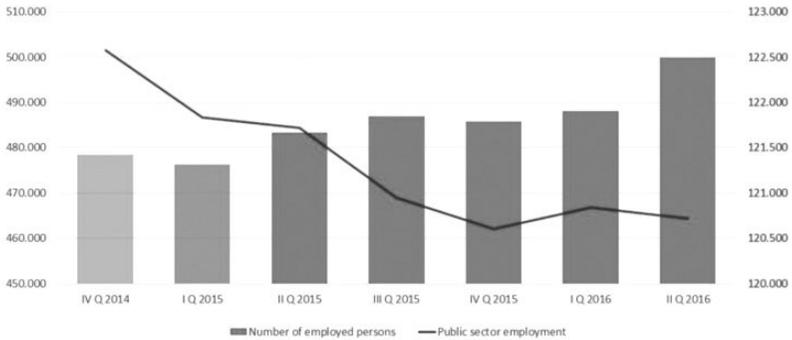
<sup>6</sup> Ministry of Finance of FBiH 2016.

**UNEMPLOYMENT IN FEDERATION OF BOSNIA AND HERZEGOVINA**



Source: Federal employment service

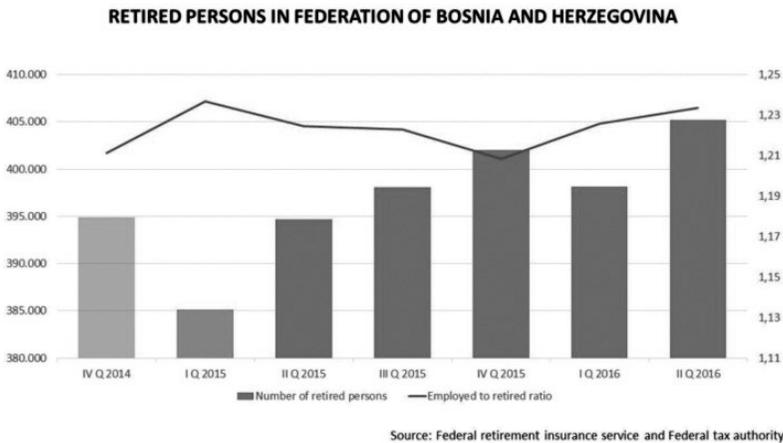
**EMPLOYMENT IN FEDERATION OF BOSNIA AND HERZEGOVINA**



Source: Federal tax authority

stagnant, so pull forces will not significantly aid in the economic growth of BiH.

When the new government of FBiH took office on March 31, 2015, the official number of unemployed was 391,663. This number decreased by 15,585, and on July 31, 2016, it reached 376,078. In accordance with the published data of the Statistics Agency of FBiH, the unemployment rate on March 31, 2015 was 46.74 percent, and on July 31, 2016, it stood at 44.77 percent. Negative trends are stopped, but for any significant



decrease in the unemployment rate, BiH needs to see growth of over 5 percent.<sup>7</sup>

On March 31, 2015, the official number of those employed, according to the tax authority of FBiH, was 476,242. That number increased by 23,178, and on July 31, 2016, FBiH had 499,420 employed persons. This net effect of an additional 23,178 newly employed, combined with other factors such as the fight against the unofficial sector of the economy has led to increase of direct tax revenues by 10.32 percent, compared with the same period last year.<sup>8</sup>

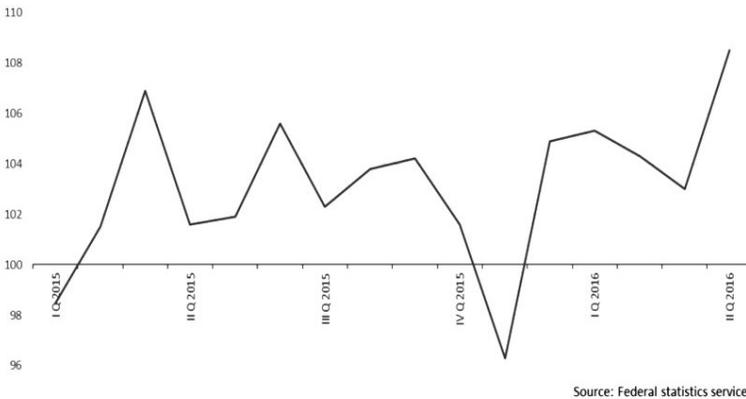
In the last quarter of 2015, FBiH experienced a large shock to its aged population. From April 1, 2015 to July 31, 2016, the number of pensioners increased by 22,086.<sup>9</sup> The magnitude of this increase is very large when taken into account the fact that the number of pensioners typically grows by 4,500-4,700 per annum. The reason for this anomaly is a change in the pension law. Specifically, the previous pension law had a penalty of 0.5 percent for each year of early retirement, whereas the new law (part of the Strategy to reform the pension system), prescribes a penalty of 4 percent per year. Thus, in only 12 months, a PR strategy caused this large increase in number of early retirements. This shock has additionally burdened the Pension Fund of FBiH for about 80 million BAM annually, and when

<sup>7</sup> Statistics Agency of FBiH, 2015-2016.

<sup>8</sup> Tax Administration Office FBiH, for the period March 31, 2015 to July 31, 2016.

<sup>9</sup> Ibid.

**GROWTH OF THE INDUSTRIAL PRODUCTION INDEX  
IN FEDERATION OF BOSNIA AND HERZEGOVINA**



added to the existing current deficit of 210 million BAM, we can see the negative impact of these events.<sup>10</sup>

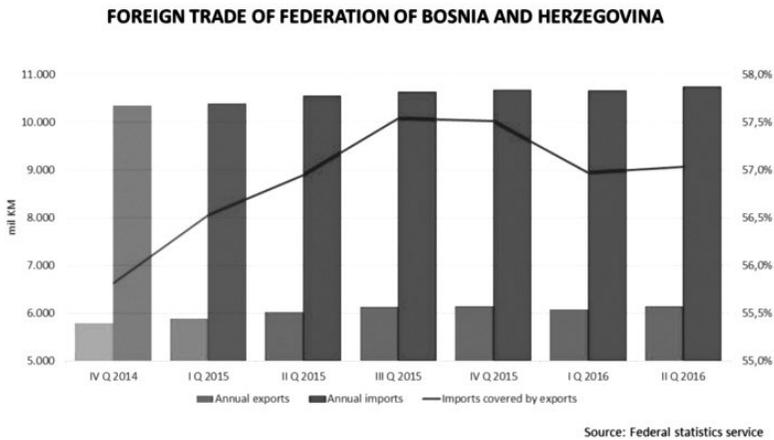
An estimated 162–165 million BAM are required for the payment of monthly pensions.<sup>11</sup> In reality, this impacts the timeline for the distribution of pensions, now about three weeks long. Basically, this is a liquidity problem. The FBiH government had initially overcome this through the so-called “overdraft,” where banks lend financial means in order for the government to be able to pay out pensions on time, after which the banks are reimbursed when contributions are collected for that month. Of course, this will come at the expense of a certain interest rate, but the government bears these additional costs because pensioners are in very difficult situations. Pensions are very low, with a minimum of 326.17 BAM, an average of 369.82 BAM, a guaranteed 434.90 BAM (if the person had worked for 40 years—full work life) and a maximum of 2,174.48 BAM.<sup>12</sup> The existing pension law does not allow for any equalization between the highest and lowest pension.

In the past 12 months, the industrial production has grown by 8.5 percent, compared to the same period last year. The prospects are that the industrial production will keep this trend.

<sup>10</sup> Institute for Pension Insurance, FBiH.

<sup>11</sup> Ibid.

<sup>12</sup> Ibid.



When it comes to trade, the volume of exports amounts to 6.1 billion BAM, and the volume of imports amounts to 10.7 billion BAM, which is a coverage of 57.03 percent, and presents the highest export-import balance in the past 4 years.<sup>13</sup>

### **Accomplished Activities by Reform Agenda Key Sectors: Public Finance, Taxation and Fiscal Sustainability<sup>14</sup>**

Budgets will be placed and maintained on a firm medium-term fiscal foundation to be agreed with the IMF in a successor arrangement to the current Stand-by Arrangement. The successor arrangement requested by BiH authorities and approved by the IMF is Extended Fund Facility. This new fiscal framework will set the public debt level on a downward trajectory, while creating room for an increase in public investment and, at the same time, reducing the size of the government sector in the economy. Fiscal consolidation will be carried out by reducing public spending and increasing public revenues, from consumption taxes, tax base expansion, gray economy and tax exemption reductions, and improvement of tax administration operations. If the above measures prove to be insufficient by the end of 2016, additional measures, including a VAT increase, will be

<sup>13</sup> Statistics Agency of FBiH, 2015-2016.

<sup>14</sup> *Update of the Action Plan for the Implementation of the Reform Agenda*, Office of the Prime Minister of Federation BiH; Last update September 16, 2016.

considered, in consultation with the IMF, on the basis of a thorough assessment, and as discussed at a high-level meeting.

### **Activities Completed by the FBiH Government:**

- **Law on the Corporate Income Tax:** The main reason for the adoption of the Law on the Corporate Income Tax is to ensure public revenues for Cantonal budgets. This is one of the FBiH fiscal system reform laws, and is compatible with other regulations, and also included IMF staff recommendations. This law aims to expand and protect the tax base, rationalize the effective tax rate without reducing the nominal, reduce avoidance and tax evasion obligations, through the definition of clear provisions, amend tax incentives covering all economic activities. The law expands the tax base in two ways: greater taxpayer coverage and greater coverage of taxable income. FBiH needs to expand the tax base and the number of tax payers, to support the fight against tax evasion and to improve overall growth. However, the tax rate of 10 percent remains unchanged and is one of the lowest in the region.
- **Amendments to the Law on Contributions:** In order to fight the gray economy and reduce liabilities, as well as to expand tax coverage, the government has approved amendments to the Law on Contributions (preferential system for low-accumulative activities). These changes enable employees from low-accumulative sectors of the economy to secure health insurance and pensions by paying contributions on a lower tax base.
- **The Initiative to Increase Road Tax on Fuel:** In order to increase the credit capabilities of Autoceste (FBiH-owned motorway company) and to accelerate the building of the highway, the FBiH government has advocated to increase the fuel road tax for an additional 10 + 5 cents (BiH fenings) per liter. It is expected that this initiative will result in law amendments, which will be passed at the state level by the end of 2016.
- **Budget Revision for 2015:** For the purpose of employment rationalization and related costs, and the implementation of fiscal consolidation measures, the FBiH government revised the 2015 budget to reduce expenses for salaries and other running costs.

- **The Initiative to Increase Excise Tax on Tobacco and Beer:** A similar model to the initiative to increase fuel road taxes. This initiative is aimed at servicing a portion of the health sector debt.
- **Amendments to the FBiH Law on Budgets:** With amendments to the FBiH Law on Budgets, the government has introduced a more rigorous fiscal rule, additional restrictions and control of lower levels of government spending, and a greater accountability of managers.
- **A Strategy for Public Debt Management:** In order to improve debt management and coordination between the entities and the Council of Ministers, the FBiH government had adopted a strategy for public debt management.
- **The Exchange of Information between Tax Administrations:** Activities to improve tax collection and to create a firmer system of information exchange between tax administrations on all levels were completed by the government in the first half of 2016.

## Employment Measures

As one of the first measures, the FBiH government introduced a moratorium on employment in this sector, which saved 13.6 percent in terms of salaries and benefits in last year's budget rebalancing. With the introduction of the moratorium, BiH decreased new hirings, and concentrated on savings deriving from the outflow of employees in public administration through the organic retirement process.

Future growth and prosperity must be based on attracting investment. There is a need to boost competitiveness by eliminating barriers to investment. In addition, there is a need to level and clear the playing field for investment by removing hidden subsidies, improving bankruptcy procedures and moving ahead with the resolution of unviable enterprises. Moreover, there are inconsistencies and complexities in the regulatory frameworks and tax systems that pose major problems for potential investors in the economy also compounded by high administrative barriers.

## Activities Completed by the FBiH Government:

As part of the activities related to the business climate and competitiveness, the following laws went through a legal procedure: The Law on Internal Payment System, the Law on Enterprises, and the Law on Foreign

Direct Investments. For the purpose of unifying and effectively planning investments in the public sector, the FBiH government has adopted the program on public investments.

- **Public Investment Program:** this program has been created to consolidate and more effectively plan investments in the public sector.
- **Law on Internal Payment System:** this law was passed to simplify payments in FBiH, and prevent tax evasion and the accumulation of debt towards the tax authority.
- **Law on Enterprises:** this law was created and adopted as a prerequisite for the use of modern methods of management, restructuring and privatization where needed.
- **Law on Foreign Direct Investments:** this law is in line with the Reform Agenda vision to base future growth and prosperity on attracting investment, and was created to ensure a more favorable climate for attracting foreign investments.

## **Labor Market**

In order to gain footing on the road to sustainable growth, Bosnia and Herzegovina must embrace its strategic advantages. These advantages include a significant potential in the workforce, which is not sufficiently utilized at present. The low activity rate of the working-age population and the high unemployment rate are the result of mismatches between supply and demand for skilled labor that restrict development opportunities. In BiH, there is a significant number of discouraged workers who are no longer actively seeking employment. Existing labor laws do not reflect the social and economic relations in BiH, and while certain provisions are contradictory to other laws, others are vague and insufficiently flexible. The culture of collective bargaining and social dialogue is underdeveloped and often burdened by unrealistic demands of social partners.

## **Activities Completed by the FBiH Government**

### ***Labor Law***

The FBiH government accomplished activities related to the Labor Law on July 31st, 2015 when the law was passed. The process of completing activities under the labor legislation was somewhat extended due to the long negotiations with social partners regarding the General Collective

Agreement, and the process of negotiations on the BCAs. It is important that the adopted law, which is favorable to both employers and employees in relation to the past, ensures that the government ends the lawsuit practice within the public sector.

### ***Decree Encouraging Employment (First Employment and Self-Employment)***

To boost the rate of employment, the FBIH government adopted the decree on first and self-employment. FBIH is the first government in the Balkans since the war to take the problem of youth unemployment seriously, and with a program of 50 million BAM distributed through cantonal employment services, collected about 7,000 job applications. In the coming months, these young people will be employed and gain essential work experience or develop in the direction of entrepreneurship. Based on the results of the implementation of the Decree, the government intends to continue with this kind of active labor policy measures in the coming years.

### ***Social Welfare and Pension Reform***

In addition to promoting initiative and efficient industry, a modern and caring society must provide for those who cannot take care of themselves. At the same time, social welfare systems must not distort incentives in the economy and must be fiscally sustainable. To achieve these ends, the governments of the Entities, Cantons and Brcko District must improve the targeting of social assistance through a set of measures that would make social protection policies more effective, efficient and equitable. Social protection needs to work for those who really need it-or who pay for it-and must be put on a sustainable financial footing. Pension systems also need to be put on a sustainable financial path if the accumulated rights of workers are to be met over the medium term.

Social security and pension reforms require a strategic approach. The following legal measures will be implemented in order to achieve results: The Law on Pension and Disability Insurance, the Law on the organization of PIO, and subsidies for electricity bills for the most vulnerable population categories. As part of the pension and disability insurance reform strategy, the Socio-Economic Council considers the draft law on the takeover of financing an outstanding contribution for pension and disability insurance. This law, among other things, addresses the issue of workers who are eligible for retirement, but are not able to realize their rights because of their companies' debts to the state.

### ***Rule of Law and Good Governance***

There is a need to ensure the irreversible entrenchment of the rule of law, which must be built on a foundation of concrete progress in the fight against organized crime, terrorism and corruption. All necessary institutional and operational developments will aim to provide citizens throughout BiH with a safer and corrupt-free environment. At the same time, government institutions on all levels will enhance their commitment to restore overall citizens' trust in the rule of law institutions by developing capacities, accountability, professionalism and integrity. Note: Activities for implementation are still at an early stage.

### ***Public Administration Reform***

Public administration reform is one of the key priorities in ensuring fiscal sustainability and the quality of public service delivery to citizens. It needs to be carried out in close relation to reforms in the socioeconomic system and rule of law.

### ***The Decree on the Regulation of the Exercise of Powers in Companies***

To enable the restructuring, privatization or liquidation of companies (53 companies), the FBiH government adopted an authorization regulation for companies with state capital from the jurisdiction of the FBiH with company categorizations. In order to systematically address the situation in public enterprises, the FBiH government has undertaken a number of measures and activities. Specifically, it has introduced the following categorization: companies of strategic interest for FBiH (18), companies for privatization (5) and companies with difficulties (29). For other companies receiving state capital, the government started activities since the beginning of its mandate.

The sale of minority stakes is in its preparatory phase. Discussions with strategic partners are ongoing in order to find the most suitable and most ideal solutions.

### ***Amendments to the Law on Civil Service, Civil Servants, and Employees***

The Amendments to the Law on Civil Service, civil servants and employees initiated the establishment of a modern, competent, more transparent, efficient, flexible as well as a more responsive public administration.

The abovementioned activities add up to 27.87 percent of the FBiH Reform Agenda Action Plan.

The FBiH government plans to fulfill the following activities by the end of this year:

- Pension Law
- Bankruptcy and Pre-Bankruptcy Procedure Law
- Amendments to the Law on Contributions
- Amendments to the Law on Personal Income Tax

The Law on Pension-insurance is a strategic law that provides a legal basis and a first step in the slow disengagement from the inter-generational solidarity. This new law will secure a transparent and simple way for pension calculation. It is a point-based system that is closely tied with each individual's monthly salary. The law aims to provide long-term financial stability to the Pension Fund, and short-term liquidity issues will be overcome by treasury system of functioning.

Bankruptcy and Pre-Bankruptcy Procedure Law will be harmonized with best practices and will offer a pre-bankruptcy procedure as an additional opportunity for the company to be bailed out. It will also prescribe more rigorous penalties for not declaring bankruptcy when conditions are fulfilled.

Amendments to the Law on Contributions will lower the contribution level to achieve a neutral fiscal effect in regards to broadening the tax base. The tax base will be expanded for non-taxable allowances, but the intention is to keep the same tax burden for the employer. In essence, this measure has two primary objectives. The first objective is to clean the system by preventing the use of non-taxable portions of the salary to increase one's wage and in this way expand the tax base, which will aid in workers' pension levels. The second objective is to mathematically lower the labor tax burden in order to show a clear picture that will attract potential investors and provide an advantage to honest employers that are reporting workers on their actual salary.

Amendments to the Law on Personal Income Tax will introduce a progressive income tax system which is widely accepted. Currently, the personal income tax law prescribes a unified tax rate of 10 percent, but it is time to move to progressive income taxation. This particular measure will be of a neutral fiscal effect, where FBiH is not trying to secure additional revenues to lower government levels but intends to place an additional

burden on higher salaries. Through this secondary redistribution of income, the government is trying to achieve additional equity.

## **Conclusion**

The key sectors and measures of the Reform Agenda are of medium term importance, meaning that the effects will be seen in the next 10-12 months. However, the immediate positive indicators are the positive reaction of employers and businesses on the changes that are taking place. The main goal is to create an attractive business environment by lowering the tax wedge, simplifying registration procedures, creating a flexible labor market, keeping social benefits at an achieved level, good governance an improved rule of law, and of course a more effective public administration.

All of this will be followed by aggressive public infrastructural projects and investments into Corridor Vc, which provides a multiplication effect of 2.4, meaning that economic growth is increased 2.4 times. F BiH will also concentrate on energy and hydropower potentials where the government expects significant investments in the medium term.

The new Extended Fund Facility program with the IMF was approved on September 7, 2016. This program is aimed at providing guidance and assistance to countries during heavy structural reform adjustments. The program itself represents the economic policy of BiH for the period 2016–19, which has three objectives:

- Accelerated reforms aimed at improving the business climate with the objective of increasing employment
- A continuous decrease in public debt to GDP ratio and a reduction in public spending in the area of public administration
- Stability of financial sector with aim to increase bank lending

Why is there such optimism in BiH? First of all, BiH reached a consensus on the most comprehensive package of socio-economic and judicial reforms the country has seen. Further, the EU and international financial institutions are ready to provide significant funds in direct support over the course of over three years in order to meet the cost of the reforms. Having an ongoing program with IFIs encourages private investment, which will boost the overall economy, creating more job opportunities. Medium term projections for economic growth (real GDP growth) for the period 2016-18 are 3.2 percent, 4.4 percent and 4.7 percent for each

of the three years, respectively.<sup>15</sup> Unfortunately, the largest part of this growth will have to be driven from within, as pull forces from trading partners are not expected to aid significantly. The projected GDP growth for the EU this year is about 1.5 percent, with no prospects of significant increases in growth next year. As for BiH, due to different potentials mainly in the sectors of energy and infrastructure, the projected growth is realistic.

If we are to consider all of the above, we can come to the conclusion that the country is harmonized, and that society has a common goal for a better life in Bosnia and Herzegovina, and of course, an accelerated path to EU accession and NATO.

In short, after two decades, without any significant economic development and still struggling to complete the process of economic transition, one can, with certainty, state that there is light for Bosnia and Herzegovina at the end of the tunnel, but in order to get there, we need everyone to be working together.

---

<sup>15</sup> BiH Directorate for Economic Planning, [www.dep.gov.ba](http://www.dep.gov.ba).

### *Chapter 3*

## **Financial Reforms in the Federation of Bosnia and Herzegovina as an Incentive for Economic Development**

*Jelka Milićević*

The current government of the Federation of Bosnia and Herzegovina (FBiH) was confirmed by the parliament on March 31, 2015. Two years into the mandate is a good time to reflect on what has been achieved so far, through the eyes of the FBiH ministry of finance. The primary goal of the incumbent government was to curb public spending growth, improve public revenue collection, and introduce a responsible management of public debt, work towards the settlement of accumulated liabilities and accumulated deficit, along with the modernization of fiscal, financial and market legislation and its harmonization with international practices, as well as the support of a business climate and private entrepreneurship. In addition to the pre-election program and the administration's principles, a significant part of the planned reforms was framed around a document called the Reform Agenda (RA), comprised of crucial benchmarks that will guide all levels of government through a four-year period. Moreover, a series of additional measures was envisaged in the letter of intent that was agreed upon by the state and entity representatives with the International Monetary Fund (IMF), whose objective is financial consolidation, market regulation reform and the advancement of economic growth.

### **Tax Reforms in the Federation of Bosnia and Herzegovina**

With the aim of adopting modern tax regulation, the FBiH ministry of finance in cooperation with the IMF, prepared a new corporate income tax law in 2015, retaining a fairly low tax rate of 10 percent. The law expanded and protected the tax base through a larger coverage of taxpayers, as well as a larger coverage of taxable income, in order to support the fight against tax evasion and to promote growth. The new law was applied in the 2016 fiscal year, and more time is required to conduct a substantial analysis of its effects. The second, and equally important reform was the

personal income tax act, which introduced progressive rates in line with the amount of income and increased tax deductions. The law is currently in the first reading phase of parliamentary procedure, followed by a public debate. Both laws are modeled after international practices and intended to bring about the harmonization of business conditions in both BiH entities.<sup>1</sup> The process of economic relief began with the simplification of processing public revenues in the FBiH, done in cooperation with USAID. The implementation of this project would see multiple benefits both for taxpayers and for the FBiH tax administration, saving time, reducing the average cost of revenue collection, and increasing the level of voluntary settlement of obligations making it easier for businesses to pay their taxes.

With technical support from USAID, the FBiH created a preliminary version of the comprehensive interactive registry of non-tax revenues, structured according to the type of fees and charges. Fully implementing the registry, control and supervision of the introduction of new non-tax revenues will be established on all levels of government, and based on it, an analysis of non-tax revenues will be carried out, which should serve as a basis for proposing reduction of existing burdens for taxpayers, triggering an increase in the employment rate and the growth of new economic investment.

## **Fiscal Stability and Public Revenue Growth**

Significant results have been achieved in maintaining fiscal stability and implementing numerous reform activities aimed at strengthening the process of European integration. The government paid particular attention to reducing the budget deficit, implementing reforms in the area of public finances, fiscal consolidation, fiscal sustainability, and strengthening institutional cooperation between all levels of government.

Through the Fiscal Coordinating Body, which has the Federal Minister of Finance as its Chairman, the FBiH Ministry of Finance and the cantonal finance ministers and representatives of the Association of Municipalities and Towns have greatly improved and deepened cooperation and communication with lower levels of government, as well as the cooperation of lower levels of government among each other. The Fiscal Coordination Body has been continuously working on the improvement and coordina-

---

<sup>1</sup> Bosnia and Herzegovina has two entities: The Federation of Bosnia and Herzegovina (FBiH), and Republika Srpska (RS).

tion of fiscal policy. Through the implementation of fiscal coordination measures and a restrictive budgetary policy, the aim is to achieve medium-term sustainability of public finances in the FBiH. The results are shown in the consolidated report described below.

Total public revenues in the Federation of Bosnia and Herzegovina include:

- Budget of the Government of the FBiH;
- Sub-entity budgets (cantons and local self-government units);
- Extra-budgetary funds (the FBiH Institute for pension and disability insurance, the FBiH Health insurance and reinsurance institute, the cantonal health insurance institutes, the FBiH Employment office and county employment services);
- Public enterprise funds (Motorway of the FBiH and Roads of FBiH) and managers for roads at lower levels of government, collected as public revenues;
- Funds of other users of public revenues in the Federation of BiH.

Total public revenues in the FBiH in 2016 recorded a growth of 9 percent compared to 2014. If only tax revenues are observed, they were realized with a growth of 13 percent or 437 million BAM. Within this category, the highest growth was recorded in the collection of corporate income taxes, which compared to 2014 were higher by more than 50 percent, or by 83 million BAM. The total collection of non-tax revenues also recorded a slight increase of 2 percent, or 25 million BAM, as well as total contributions of extra-budgetary funds, which are higher by 7 percent, or 192 million BAM.<sup>2</sup>

In 2016, all levels of government in the FBiH achieved a positive financial result in the consolidated amount of 124.4 million BAM. The budget of the Federation of Bosnia and Herzegovina reached a surplus of 85 million BAM, the cantonal budgets had a surplus of 21.5 million BAM, and the municipal budgets a surplus of 27.5 million BAM. The FBiH government has, despite an inherited accumulated deficit of 173 million BAM at the end of 2014, through a two-year positive budget execution, the entire amount of accumulated deficit has been rehabilitated. Thus, at the end of 2016, for the first time in over ten years, the FBiH recorded an accumulated surplus in its budget. At the very beginning of their mandate, the FBiH

---

<sup>2</sup> FBiH Ministry of Finance.

**Table 1. Consolidated overview of total public revenues in the FBiH: 2014–2016**

Consolidated Table – Federation of Bosnia and Herzegovina in BAM millions

TITLE	2014	2016	Difference	Index
I. Tax income	3.268	3.705	437	113
1. Income from indirect taxes from the Single Budget Account	2.689	2.971	282	110
2. Toll-based revenues 0.10 BAM / L for highways	63	76	13	121
3. Corporate Income tax	163	246	83	151
4. Personal Income tax	277	315	38	114
5. Taxes of citizens	75	97	22	129
II. Non-taxable Income	1.009	1.034	25	102
1. Fees, fines, and other non-taxable income	498	502	4	101
2. Special fees	160	199	39	124
3. Federal fees for the use of roads	25	29	5	119
4. Other non-taxable income, out of:	327	304	-23	93
Dividend	167	78	-89	47
End-user revenues	110	192	83	175
Other	50	33	-17	66
Total tax and infringement revenue (I + II)	4.277	4.740	463	111
III. Extra-budgetary Funds	2.790	2.983	192	107
1. Contributions for pension and disability insurance	1.548	1.647	99	106
2. Contributions for health insurance	1.116	1.200	84	108
3. Unemployment insurance contributions	127	136	9	107
Total (I + II + III)	7.068	7.722	655	109

NOTE: Included in the amounts presented is a part of the revenues intended for repayment of external debt. The revenue plan does not include the proceeds of privatization and grants.

government implemented significant cuts in public sector wages and overall government employees, by limiting new government employment, drastically bringing down expenses.

In 2017, the FBiH ministry of finance developed a strategy for public finance management for the period 2017–2020. The aim of this strategy was to provide a comprehensive and integrated framework for planning, implementing, and monitoring the implementation of reforms. The goal was to improve macroeconomic stability, ensure the efficient and targeted

use of public resources, and improve the services provided by the state administration. At the same time, they aimed to increase the accountability, efficiency, transparency, and functionality of public finance management, and fulfill the necessary conditions for joining the European Union. The strategy is divided into six key pillars and includes a sustainable medium-term macro-fiscal and budgetary framework, revenue mobilization, budget planning, a plan for budget execution, the introduction of effective internal controls, and the provision oversight of public finances through external audits.

In addition, in 2016, the ministry issued a “manual for the preparation of a statement on the fiscal assessment of laws and planning acts on the budget,” which ensured the timely planning of expenditures for implementation of regulations and planning acts, and the inclusion of fiscal estimates in budgetary processes. By adopting this rulebook, stipulating the forms on which a statement on the fiscal assessment of regulations is issued, their implementation is closely related to the economic classification of the budget and sources of financing. This, among other things, provides the ministry of finance better control of the assessment of fiscal effects on the budget. The rulebook is one of the key instruments of good fiscal governance that enables the forecasting and control of future spending, thereby retaining or even reducing the level of public expenditures. Such an assessment has increased the transparency of the decision-making process, providing information on the potential fiscal consequences of the application of a particular regulation.

## **Public Debt Management**

This FBiH government has completed the task of curbing the growth of public spending and preventing the further growing of the public deficit. In March 2017, the public debt of the FBiH amounted to 6,201.92 million BAM, a reduction of approximately 47 million BAM from two years prior. This data is especially important considering the FBiH recorded significant GDP growth, while under the previous government, the public debt increased for 1.5 billion BAM. Since October 2015, the FBiH ministry of finance has regularly published quarterly reports on the debt levels.

In the first year of its mandate, a medium-term debt management strategy was adopted in order to define strategic debt management guidelines, optimize risks and borrowing costs, and increase the transparency of borrowing operations. Furthermore, the ministry has, as of 2016, published

an annual plan of borrowing operations. This transparency has shown positive results, with increased investors responses and low borrowing costs, and most importantly, with timely insurance of the planned funds needed for efficient liquidity management of the budget.

Despite many inherited problems, all parameters show that the FBiH ministry of finance has been implementing a very cautious and transparent borrowing policy. In order to continue this positive trend and prevent excessive public debt creation in the near future, the ministry has prepared a completely new legal framework for public sector debt in the Federation of BiH in order to establish stricter fiscal rules and more effectively manage the total public debt in FBiH. They plan to finalize the draft law on debt, send it to the government for consideration, and then to the parliament to be adopted during regular proceedings.

## Preparation of Laws and Other Regulations

Through parliamentary procedure, the ministry has prepared and implemented more than 20 laws in the last two years. Some of them are brand new, while others are amendments to existing laws.

A few of the important laws:

- **The law on internal payment transactions** prescribes the execution of internal payment transactions in the FBiH, determines participants and organizations authorized to perform payment operations, defines the types of accounts, the methods of payment, rights and obligations for internal payment transactions.
- **The factoring law** regulates factoring, defines the types of factoring, factoring contracts, conditions for the establishment, operation and termination of factoring companies, risk management, financial reporting, as well as auditing and supervision of the operations of factoring companies.
- **The financial operations law** regulates the issues related to the basic rules of financial operations, the obligations of the administration and the supervisory board in the conduct of the entrepreneurs, taking measures for liquidity insurance, the risk in financial operations, the deadlines for the execution of monetary liabilities of entrepreneurs and public law entities, legal consequences of delays in the performance of monetary obligations, the nullity of certain provisions of the contract on business transactions, as well as the obligations of

the entrepreneur in the event of illiquidity, and the supervision of entrepreneurs and public law entities.

- **The law on amendments to the law on a unified system of registration, control and collection of contributions** was adopted with the aim of suppressing blackmail and increasing discipline in the field of contributions. The legislation was prepared by the tax administration in cooperation with the USAID FAR project.
- **The law on banks** was adopted with the aim of raising the level of resilience of individual banks, as well as the overall banking system in order for capital-enhanced banks to provide more support to the real sector and to establish a comprehensive legal framework for bank restructuring aligned with international banking standards.
- **The insurance act** regulates the insurance market in the FBiH following EU standards.
- **Treasury act** is a revised and updated version of the Treasury act (2002), which prescribes the introduction of a treasury system and operations through a single account for all municipalities, cities and extra-budgetary funds in the FBiH region.
- **The law on games of chance** regulates the market in the field of games of chance, improves the financial discipline of business entities, and establishes an efficient and reliable system of supervision and control of the entire business and the realized turnover of the game organizers of games of chance.
- **The law on voluntary pension funds** creates the legal basis for the further development of the pension system in the FBiH and the capital markets where new types of funds will appear, which differ in the way and criteria of investment.
- **Financial management and control act** is based on risk management and is introduced to improve financial management and decision-making in the realization of the organization's objectives, such as compliance with business regulations, plans, contracts, and policy procedures. It also provides protection of assets, liabilities, and other resources from losses that may result from poor management, unreasonable consumption and use, and protection against irregularities, abuse, and fraud.
- **The law on amendments to the law on internal audit in the public sector** implements reforms in the field of internal audit in accordance with the international standards of professional practices

of internal audits, published by the International Institute of Internal Auditors, as well following best practices from EU member states.

The parliament should soon have a second reading, the Accounting and Auditing Act, which improves the quality of financial reporting, encourages professional behavior of accountants and auditors, facilitates public access to information on the company's performance and financial position, and generally increases public confidence in the accounting profession.

The Law on the banking agency is expected to be passed soon. The parliamentary procedure is undergoing for the law on contributions, and the law on microcredit organizations, the law on compulsory insurance in transport, and the law on development banks.

A special thanks, for the creation, and often also the implementing of laws, goes out to international institutions, in particular the IMF, the World Bank, and government agencies, such as the USAID and the Swedish SIDA. The international experience the IMF is offering through its technical assistance, or USAID's municipal treasury projects, are important support mechanisms in our reform process.

## **Economic Trends**

While the previous part of this chapter mainly dealt with initiatives by the FBiH ministry of finance, this last part will focus on indicators from the private sector, comparing results in 2014 and the same period in 2016.

The data that follows is the result of aggregated data and balance sheets annually submitted by taxpayers to the Financial Information Agency. The total number of business entities operating in the FBiH region recorded a slight increase of about 2.2 percent between 2014–2016. This trend is accompanied by a positive balance of newly registered companies in relation to those that closed down.

However, although the growth of active companies is not high, the results of the business have a stronger positive trend. The value of operating revenues in 2016 amounted to more than 42.4 billion BAM, which is an increase of 2.1 billion BAM from two years prior.

The structure of operating revenues is dominated by revenues generated on the domestic market, while the share of export revenues in total revenues is relatively modest. However, in the observed period, export earnings recorded growth, both by value and by share.

**Table 2.**

<b>Subjects</b>	<b>2014</b>	<b>2016</b>
Economy (total)	21.401	21.875
Small	18.401	18.813
Medium	2.292	2.325
Large	708	737
Banks	38	34
Insurance companies	16	17
Total	21.455	21.926

Source: The FBiH ministry of finance / Financial Information Agency.

**Table 3.**

	<b>2014</b>	<b>2016</b>
Value of export earnings (BAM)	5.984.302.403	6.479.931.945
Share in business income (%)	14,84%	15,24%

Source: The FBiH ministry of finance / Financial Information Agency.

**Table 4.**

<b>Year</b>	<b>2014</b>	<b>2016</b>
Fixed assets (BAM)	37.911.531.119	38.643.740.074
Current assets (BAM)	19.869.107.279	20.805.363.956
Total assets (BAM)	60.176.460.355	61.706.235.266
Capital (BAM)	30.828.890.772	31.756.091.247
Long-term liabilities (BAM)	9.291.366.548	9.096.100.676
Short-term liabilities (BAM)	17.444.565.503	18.360.704.379

Profitable companies (12,570, or about 60 percent of the total number of active companies) generated 2 billion BAM and 230 million BAM in net profit in 2016, which is 13.03 percent more than the profit realized two years earlier (1.97 billion BAM). At the same time, the number of loss-making companies also decreased (from 6,712 in 2014 to 6,120 in 2016), and total losses also declined (from 1.6 billion BAM in 2014, to 990 million BAM in 2016).

Such generally positive business trends in companies in the Federation of BiH resulted in an increase in the value of assets, as well as capital, which are available for creating new value. The total value of corporate assets increased from 60.18 billion BAM in 2014 to 61.71 billion BAM in

2016, an increase of 2.54 percent. The growth of current assets is somewhat more intense than the growth of fixed assets—4.7 percent, compared to 2.54 percent. The value of equity capital (share capital in joint stock companies and shareholders' equity in limited liability companies), which finances the business activity of companies in the Federation of BiH in the observed period, increased by 3.0 percent, from 30.83 billion to 31.76 billion BAM.

As expected, the number of employees in FBiH companies is growing, from 309,982 in 2014 to 326,155 at the end of 2016. As a result, employment grew by 5.22 percent over this period. Salaries also grew, with average monthly salaries in 2014 standing at 833 BAM, while in December 2016 they increased to 861 BAM.

## **Conclusion**

The Federation of BiH is still a young market, burdened with difficulties of post-war recovery, a complex political structure, and slow eradication of corruption. More than 10 billion BAM-worth of bank deposits indicate that there is space for further investment of capital. There is no doubt that it is a strong priority of BiH authorities to continue creating a welcoming climate for the development of a private sector entrepreneurship, with the market, not the state, as the leading actor. Important steps have been taken, but they need to be further expanded and developed. Eliminating para-fiscal charges, facilitating the registration of economic entities, computerization and digitization of businesses will open ways for creative entrepreneurship, increased employment, and economic growth.

## *Chapter 4*

# **Cost-Benefit Analysis for the Establishment of the Ministry of Agriculture, Food, and Rural Development of Bosnia and Herzegovina**

*Sanela Klarić, Mubidin Zametica, Emir Klarić,  
and Selma Osmanagić Agović*

After years of stagnation in the Agriculture and Rural Development sector of Bosnia and Herzegovina (BiH), the following cost-benefit analysis, arguing for the establishment of a BiH ministry of agriculture, food and rural development, represents a logical and natural continuation of efforts to draw attention to the ministry, and argue for its necessity.

Experts, institution representatives, the academic community, civil society organizations (CSOs) in the rural development sector, and farmers have clearly demonstrated that only by strengthening the institutional framework on the state level through the establishment of a functional ministry of agriculture, food, and rural development, fundamental changes can be made toward advancing and improving this sector. In the last decade, efforts to coordinate between different levels of governance have been futile and discouraging, and there cannot be a functional solution in the future without the establishment of such an institution.

In general, the agriculture and rural development sector in BiH is characterized by insufficient institutional capacities, jurisdiction overlapping, undefined chains of communication and control in almost all spheres of agriculture, weak communication, coordination and information exchange between different levels of governance, and unsynchronized systems of subsidies on different administrative levels. In addition, subsidies for this sector are insufficient and are not harmonized with the agricultural policy of the European Union.

The making of important strategic agricultural and rural decisions is complicated due to a lack of basic information on the sector, quality mining and processing of data on agriculture, as well as a lack of reliable statistics and cooperation between data indicator agencies. Such information is necessary for farmers to adequately place their products on the market.

Moreover, the lack of information discourages foreign investors to set up development projects in BiH.

Due to a failure to establish IPARD (Instrument for Pre-Accession Assistance in Rural Development) structures (an IPARD payment agency and governing body, and the creation of a state strategy for the rural development), BiH has thus far not been able to use the 2007–2013 IPARD funds for agriculture and rural development that are given directly to farmers and rural communities. If decision-makers fail to agree on the establishment of the above-mentioned structures, BiH will be unable to access the funds for the planned period of 2014–2020. Moreover, due to the tardiness in implementing measures and activities on the mitigation of consequences of Croatia's accession to the European Union (EU), BiH has brought into question the export of products of plant and animal origin from BiH after Croatia's accession into the EU, thus directly jeopardizing the position of farmers and producers from BiH on foreign markets and the overall economic progress of the state.

The implementation of reforms leading toward European integration is conducted very slowly in BiH. Preparations in these areas are still in an early stage, and visible progress was made only in the field of food safety and veterinary policy. In the coming year, BiH should focus on the following: aligning the official veterinary and phytosanitary control system with European standards, strengthen its administrative capacity and in particular its inspection services and laboratories, drawing up a State-level strategic plan for rural development, and establishing national structures for pre-accession assistance to the agricultural sector through the Instrument for Pre-accession Assistance for Rural Development.<sup>1</sup> This study has found that a solution for the general discord and absence of coordination in the implementation of agricultural policy in BiH should be sought in the strengthening of the institutional organization and the state-level jurisdiction.

The cost-benefit analysis provides specific answers to the question of the costs for the establishment and maintenance of this ministry and, on the other hand, which benefits and advantages farmers and citizens can expect. So far, such answers have been missing to complete the argumentation in the advocacy for the establishment of this ministry. Keeping in

---

<sup>1</sup> "European Neighbourhood Policy And Enlargement Negotiations." European Commission. [https://ec.europa.eu/neighbourhood-enlargement/pdf/key\\_documents/2015/20151110\\_report\\_bosnia\\_and\\_herzegovina.pdf](https://ec.europa.eu/neighbourhood-enlargement/pdf/key_documents/2015/20151110_report_bosnia_and_herzegovina.pdf).

mind Bosnia and Herzegovina's large public administration on all levels of government, the matter of establishing a ministry of agriculture, food, and rural development on the state-level should be approached in a serious and studious manner, which will result in the answers to the above-mentioned questions.

## **Research Methodology**

In the following analysis, our research team used both quantitative and qualitative research methods. The research team conducted a considerable number of interviews with representatives of institutions on various levels of governance, as well as with local and international experts and civil society organizations (CSOs). In addition, best practices from countries in the region were consulted (Croatia and Macedonia in particular), establishing an institutional framework in the sector of rural development, and experiences from these countries adapted to the needs and context of BiH. Furthermore, preliminary study results were presented to the CSOs working in the rural development sector, chambers of commerce, and other stakeholders during two regional meetings in Livno and Trebinje. These meetings and subsequent discussions aimed at testing the research hypotheses, presenting the preliminary results of the cost-benefit analysis, and getting an overview of positions of interested parties on a wider spectrum.

Cost-benefit analysis (CBA) is a method in economic analysis that evaluates and compares all benefits and flaws of a project that could arise from project implementation.<sup>2</sup> The emphasis is on a systematic overview and comparison of costs and benefits that are the result of an investment project within the overall societal context. In addition, it takes into account a number of social and economic parameters in order to determine the societal benefits and losses that may result from project implementation.

Since this cost-benefit analysis is atypical—being an analysis in support of establishing a ministry of agriculture, food, and rural development of BiH and all costs and benefits pertaining to it—special attention has been given to those factors that are considered difficult to monetize, so that the baseline of a cost-benefit *analysis* can be accomplished, which implies that it is necessary to include as many financial, economic and social factors as

---

<sup>2</sup> Milan Čupić, "Cost-benefit analiza" (Cost-Benefit Analysis), Business Start-up centre Kragujevac, 2009.

possible, in order to adequately approach the assessment of the project's cost-efficiency. Therefore, the financial and economic analyses have been complemented by a multi-criteria analysis, taking into consideration multiple criteria and their evaluations.

## **Contextual Analysis of Establishment of the Ministry of Agriculture, Food, and Rural Development of Bosnia and Herzegovina**

We have noted in the introduction that this cost-benefit analysis in support for the establishment of the ministry of agriculture, food, and rural development of BiH represents a logical and natural continuation of efforts made by experts, representatives of institutions, the academic community, civil society organizations (CSOs) in the rural development sector, and farmers, in order to draw attention to the urgent need for establishing such a ministry and to advocate it with sound arguments.

The following part provides an overview of current challenges in the sector of agriculture and rural development, in terms of the institutional and legislative framework, cooperation of institutions in charge, as well as the way it reflects on the European integration process, with special emphasis on the issue of under-preparedness of BiH for Croatia's EU membership. In addition, we will provide a short overview of the agricultural policy in the EU, its standards, and the relevant structures.

## **Institutional and Legislative Framework for Agriculture and Rural Development in BiH**

The institutional framework for agriculture and rural development has been regulated in a way that the majority of jurisdictions in the sphere of agriculture and rural development are given to the entities and the Brčko District (BD). Hence, at the entity level two ministries and a department are in charge of governing the sector of agriculture and rural development: Republika Srpska's Ministry of Agriculture, Forestry and Water Management (MAFWM-RS), the BiH Federal Ministry of Agriculture, Water Management and Forestry (FMAWF), and the Department for Agriculture, Forestry and Water Management in BD. The situation is further complicated at the level of FBiH, where administrative bodies in charge of agricultural, veterinary, forestry- and water management-related issues, are established separately in all 10 cantons.

At the state level, the jurisdiction in the field of agriculture and rural development is assigned to the Ministry of Foreign Trade and Economic Relations of BiH (MoFTER BiH) and has been defined by the Article 9 of the Law on Ministries and Other Governing Bodies in BiH.<sup>3</sup> MoFTER BiH is in charge of the cooperation with the EU and other international organizations that are relevant for the sector of agriculture, food, and rural development, international agricultural trade, the creation of a unique economic market, general legislation, custom control measures and inspection supervision in the veterinary sector, animal identification and harmonization of policies made by entity institutions, and governance with international policies. In this regard, the sector for Agriculture, Food, Forestry, and Rural development exists within the scope of MoFTER BiH.

MoFTER also encompasses administrative organizations; the State Veterinary Office of BiH (SVO BiH) and the Administration of Bosnia and Herzegovina for Plant Health Protection (APHP BiH), which have their own jurisdictions in matters of animal health care and plant health. These administrative organizations report directly to the minister, while the Sector for Agriculture, Food, Forestry, and Rural Development is in charge of the coordination for these administrative units. MoFTER BiH includes an additional administrative unit, the Office for Harmonization and Coordination of Payment Systems in Agriculture, Food, and Rural Development in BiH, which is, among other things, authorized to develop a legal framework for the establishment and development of institutional structures to support the policy implementation measures and attracting funds from EU other international agencies, and to establish unique practices and procedures of approval, implementation, and accounting transactions in the sector of agriculture, food, and rural development, which are to be applied in the entities and the BD. Apart from that, the jurisdiction over the matters of food safety at the state level is given to the Food Safety Agency of BiH (FSA BiH). FSA BiH is an independent administrative organization, under the jurisdiction of the Council of Ministers of BiH (CoM BiH), which cooperates with the MoFTER BiH in food-related issues.

Considering the complexity of this administrative set-up and the division of authorities in the sphere of agriculture across different levels, as well as the administrative units that MoFTER BiH is expected to oversee,

---

<sup>3</sup> Law on Ministries and Other Governing Bodies in BiH, Official Gazette of BiH, issues 5/03, 42/03, 26/04, 42/04, 45/06, 88/07, 35/09, 59/09 and 103/09).

it is quite understandable to conclude that this sector and its capacities have been reduced in the past two years.<sup>4</sup> This is particularly relevant when taking into account the context of liabilities arising from Bosnia and Herzegovina's accession to the EU.<sup>5</sup> When it comes to coordinating administrative organizations from the part of the Sector for Agriculture, Food, Forestry, and Rural Development (where there is currently only one work position that coordinates the operations of APHP BiH, SVO BiH and FSA BiH), we can conclude that in such circumstances coordination cannot be successful and that it should be improved. Furthermore, a question is raised in regard to the hierarchical organization within the Ministry and the administrative units that the Sector is supposed to coordinate, i.e., the feasibility of a coordination of units administered by the chief managers, which is done by the Sector (state office) that is governed by the assistant to the minister. This is where challenges arise in coordinating and achieving a quality, quick, and effective communication, which is why it has been clearly demonstrated that the Sector for Agriculture, Food, Forestry, and Rural Development, with its current capacities, is not in a position to meet its law-prescribed responsibilities.

When it comes to the legal framework, the Law on Agriculture, Food, and Rural Development of BiH<sup>6</sup> regulates the basic aims, principles and mechanisms for the development of policies and strategies, structure, and jurisdictions on all level of governance, their functions and liaisons, mechanisms of monitoring and assessment, as well as their administrative supervision. This law is also supposed to facilitate the progress of European integration and sector harmonization, as well as the phases of preparation for establishing pre-accession funds. However, the law does not foresee any control mechanisms or consequences for authorities that fail to meet their duties. Furthermore, the process of creating the strategy for rural development at the state level was formally launched, but stopped very quickly. The creation of a strategy for rural development, the advancement

---

<sup>4</sup> This sector presently employs only 25 persons and many professional spheres of the agricultural and rural development sector are not represented.

<sup>5</sup> Coordination has been additionally complicated and slowed down with the establishment of the Republika Srpska Ministry for Economic Relations, which represents an equivalent to the Direction for European Integrations (DEI) at the entity level, through which the entire communication related to the EU integrations needs to be made. Understandably, this ministry does not employ experts for every individual field, including agriculture and rural development, and therefore its employees cannot respond promptly and offer opinions on a given topic. Instead they seek additional counseling with authorized bodies, which further slows down the work that is already slow and poorly coordinated.

<sup>6</sup> Official Gazette of BiH, issue 50/08.

of IPARD structures and the creation of an IPARD program, based on that strategic plan, have been the objectives of several already financed projects by the EU IPA funds.<sup>7</sup> However, the lack of political will for the adoption of the above-mentioned documents and structural developments at the state level led to these projects failing to accomplish their objectives, thus leaving the funds from the IPARD program unused. BiH remains deprived of a strategic document and a necessary structure as the basis for IPARD programming.

There is currently a strategy of rural development in RS, while in FBiH the process is underway to create an operative plan of rural development for 2014–2020. One of the conditions for BiH to access the IPA 2 program for 2014–2020 is to reach an agreement on creating a comprehensive long-term state strategy for rural development, forming IPARD structures, and implementing IPA measures of rural development in accordance with the demands set by the IPA for the state strategy and rural development program.

## **General Features of the State of Agriculture in BiH and the EU Integration Process**

The state of the agricultural sector in BiH is characterized by varying legal regulations in different areas, legal overlapping, limited capacities and communication channels, and a lack of clear vision and necessary reforms. At the state level, there are no defined agricultural policies in a real sense, although Chapter II of the Law on Agriculture does define general objectives and measures of the policy of agriculture, food, and rural development and its stakeholders. The agricultural policy is currently being conducted at the entity and BD level, but the scope and effects of such policy are limited. Domestic production and local farmers do not receive sufficient incentives and are not protected, since BiH does not have measures of protecting domestic production from excessive imports of certain products, which has its legal ground in CEFTA.<sup>8</sup> In fact, although

---

<sup>7</sup> Support for Implementation of the Functional Review Recommendations in the Agriculture Sector (SESMARD), 2006–2008 (financed through CRDS funds in the amount of 1 million euros), IPA 2007, Strengthening the BiH Rural Development Programming Capacities (3P-BHRD) 2009–2011, in the amount of 2.2 million euros.

<sup>8</sup> CEFTA stands for Central European Free Trade Agreement, which has been signed in December 1992 by then Czechoslovakia, Hungary, and Poland. Slovenia became a member of CEFTA in 1996, Romania in 1997, Bulgaria in 1999, Croatia in 2003, and Macedonia in 2006. The main objectives of CEFTA were: harmonizing the development of economic

the CEFTA Agreement and the Stabilization and Association Agreement with the EU both foresee certain options for the protection of local products when local markets are threatened, so far no steps have been taken to enact these in the country. The result of such passive politics is the inability to sell local products in the domestic market, decreasing incentives for local production.<sup>9</sup>

The rate of import liberalization is unprecedented in our region, which is evident in the fact that within the CEFTA association, only BiH has a zero-custom rate for all products, while other countries maintain concessions on products that are of special interest to these countries. Besides, BiH has entered these arrangements with its institutions entirely unprepared to establish reciprocal non-custom measures and ensure the export of its products to the demanding market of the EU. MoFTER BiH and CoM BiH have not developed measures for the protection of local production from excessive import of certain products, which is a fact that has its legal ground in CEFTA. Such a position in foreign trade is not in BiH's economic interest, and, above all, is detrimental for its agricultural sector.<sup>10</sup>

Strategic decision-making in the agricultural and rural development sector is complicated due to a lack of basic information on the sector, quality mining and information processing on agriculture, and the absence of reliable statistics and cooperation between statistical entity agencies. More precisely, BiH has still not adopted an informative agricultural strategy or a law on agricultural census. Lacking necessary information and a sense of security for investing, this unclear and disordered state of the

---

relations, providing equal commercial treatment and removing obstacles to trade between signatory countries. Furthermore, CEFTA functioned as one of the preparatory activities of signatory countries on their way toward a full membership in the EU. Therefore, the signatory countries set the following conditions for accession to CEFTA: a signed EU accession agreement, membership in World Trade Organization (WTO) and the approval of all established members of CEFTA. Once becoming members of the European Union in 2004, the Czech Republic, Hungary, Poland, Slovakia, and Slovenia withdrew from CEFTA. In 2004, the remaining members were Bulgaria, Romania, Croatia, and Macedonia. Since May 1 2007, members include: Albania, Bosnia and Herzegovina, Montenegro, Croatia (Croatia's membership in CEFTA ended 24 hours before its EU accession), Macedonia, Moldova, Serbia, and Kosovo (UNMIK). More on the matter can be found at: <http://www.dei.gov.ba/dokumenti/?id=4553>.

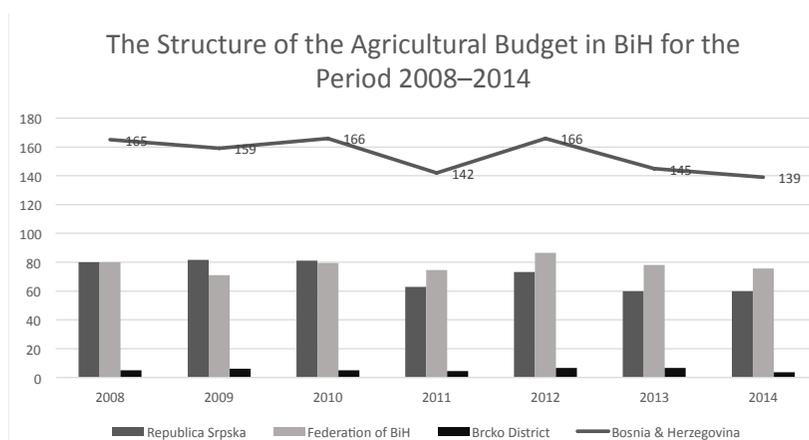
<sup>9</sup> More on the matter can be found at: "Poljoprivreda i ruralni razvoj u BiH—Preporuke civilnog društva za brži EU" (Agriculture and Rural Development in BiH—Civil Society Recommendations for a Faster Way Toward the EU), [http://gradjanizaeuropu.ba/sites/default/files/poljoprivreda\\_i\\_ruralni\\_razvoj\\_finalne\\_preporuke\\_gradjana\\_zaeuropu.pdf](http://gradjanizaeuropu.ba/sites/default/files/poljoprivreda_i_ruralni_razvoj_finalne_preporuke_gradjana_zaeuropu.pdf)

<sup>10</sup> Ibid.

agricultural and rural development sector fails to attract foreign investors and new business ideas.<sup>11</sup> This also complicates the process of accession into the World Trade Organization (WTO) and further thwarts negotiations with the EU related to agriculture.

The total allocation for agriculture on all administration levels in 2014 reached its lowest level in a six-year period since 2009. In 2014, the total allocation stood at 139.1 million BAM, which represents a decrease of 5.6 million BAM or 4 percent when compared to the previous year's budget of 145.05 million BAM.<sup>12</sup> In 2014, the budget decreased by about 16 percent from 2012, when the total allocation was highest.

**Figure 1. Overview of total allocations into agriculture in BiH (in millions BAM)**



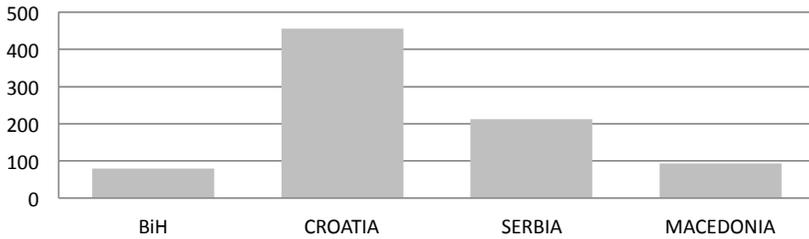
Source: Ministry of Foreign Trade and Economic Relations of BiH<sup>13</sup>

<sup>11</sup> It is worth noting that through its IPA 2007 project “Strengthening and Harmonization of BiH Agriculture and Rural Sectors Information System” the EU gave technical support to BiH with the aim of advancing the collection of ordered and reliable data from rural economy and agricultural sector, based on a methodology that is standardized and harmonized with the EU and developed during the implementation of a pilot-project for collecting data on agricultural production, economic operations on farms and accessibility of correct information and sampling. Within the course of this project, different strategic documents and analyses had been made that were never adopted due to the lack of political will.

<sup>12</sup> Agricultural Report for BiH, 2012, Ministry of Foreign Trade and Economic Relations, May 2013, available at: [http://www.mvteo.gov.ba/izvjestaji\\_publicacije/izvjestaji/default.aspx?id=7577&langTag=bs-BA](http://www.mvteo.gov.ba/izvjestaji_publicacije/izvjestaji/default.aspx?id=7577&langTag=bs-BA)

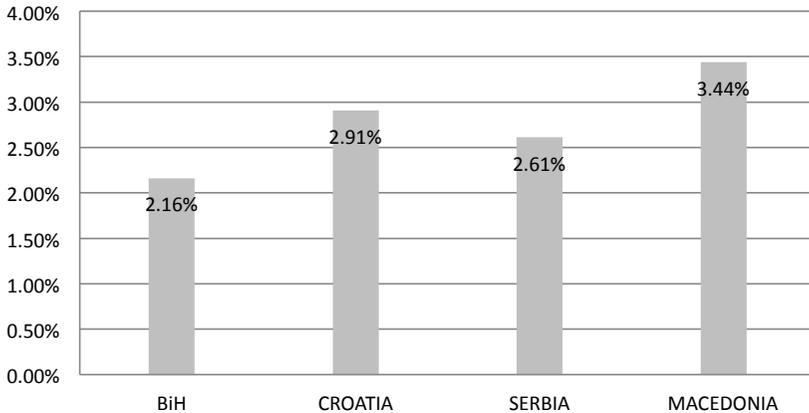
<sup>13</sup> Ibid.

**Figure 2. Investment into agriculture in countries in the region (millions of euros)**



Source of information: Ministry of Foreign Trade and Economic Relations of BiH<sup>14</sup>

**Figure 3. The rate of the investment into agriculture in the budgets of countries in the region (%)**



Source: Authors.

In order to get a realistic image of the level of support given to farmers in BiH, a comparison has been made of budgetary support in BiH with that of other countries in the region. The level of support given to agriculture and rural development in BiH is well below that of countries in the region which BiH has trade partnerships with. Based on a comparison for a five-year period, it was determined that in the time period between 2008 and 2012, Croatia received the highest level of support in the region with an average of 456.3 million euros. Serbia followed with 212.3 million

<sup>14</sup> Agricultural Report for BiH, 2012, Ministry of Foreign Trade and Economic Relations..

euro, Macedonia with 93 million euros, while Bosnia and Herzegovina is last with an average of 80.6 million euros.

When this investment is represented in percentage terms of total budgets, the highest rate of allocation was recorded in Macedonia, where it represented 3.44 percent of the total budget, followed by Croatia with 2.91 percent and Serbia at 2.61 percent.

Concerning investments trends, it can be noted that the most positive trend is exhibited by Macedonia, which has increased its investment into agriculture by 90 million euros from 2008 until 2012 (from 45 million euros in 2008 to 135 million euros in 2012), while the other three countries (BiH, Croatia, Serbia) displayed a more or less stable allocation level. Taken into account the levels of budgetary support and of local agricultural production, it is clear that in comparison to producers in neighboring countries, the agricultural producers in BiH are in a disadvantaged position.<sup>15</sup>

All above-mentioned factors hamper the operations of the agricultural and rural development sector. Consequently, the sector lags behind with the EU accession process in terms of its harmonization with the legal acquisitions of the EU, its procedures, and requested structures that are to implement the development policies in the sector. The lack of institutional capacities for development, coordination, and monitoring of agricultural policies and legislation is a large obstacle to a fast development of the local agricultural sector. This lag primarily reflects itself on the economic state of BiH citizens.

## **Agricultural Politics in the EU, Standards, and Programs of Support**

The agricultural policy has always been one of the most important EU policies and was raised to the level of the Union as the Common Agricultural Policy (CAP), which defines the standards for participating in a common agricultural market for all member countries. Since its adoption, the common market and reduction of technical obstacles to trade have significantly contributed to trade increase of food products in Europe.<sup>16</sup> Policies

---

<sup>15</sup> Agricultural Report for BiH, 2012, Ministry of Foreign Trade and Economic Relations..

<sup>16</sup> Bruno Henry de Frahan and Mark Vancauteran, Harmonisation of food regulations and trade in the Single Market: evidence from disaggregated data, p. 33 *European Review of Agricultural Economics*, p. 337, pp. 337–360 (2006), in “Standardi Europske Unije za državnu regulaciju poljoprivrede” (Standards of the EU for State Regulation of Agriculture), available at:

concerning the coordination, harmonization, and competitiveness have always been prioritized by decision-makers in the EU, and are illustrated by the fact that the agricultural legislature of the EU accounts for over 50 percent of total legislature. In addition, an important indicator of the significance of this sector at the EU level is the EU's investment in the agricultural sector. Namely, almost 35 percent<sup>17</sup> of the EU budget is allocated to agriculture and rural development, while, as it was previously noted, BiH allocates only around 2 percent to this sector.

Since the beginning of the EU accession process, it has been recommended to BiH to form a ministry of agriculture, food, and rural development, which would provide a clear and developed coordination of complex policies of agriculture and rural development.

In order to receive membership to the EU, countries must adopt and effectively implement the EU *acquis*, which refers to the entire European legislative body<sup>18</sup>. Chapter 11 of the EU *acquis* contains the Common Agricultural Policy (CAP), which regulates the European market for agricultural products.<sup>19</sup>

More specifically, in order to proceed with EU accession, BiH will have to implement the CAP. As part of this implementation process, the EU highlights the following:

- Development of a uniform administrative structure;
- Data-mining;
- Subsidy administration;
- Food safety;
- Veterinary policy and policy on plant health;
- Rural development.

---

<http://www.mreza-mira.net/wp-content/uploads/EU-standardi-za-regulaciju-poljoprivrede.pdf>

<sup>17</sup> In the 1970s this amount was even higher and the total rate of financing of agricultural policies accounted for around 70 percent of the total EU budget. The reduction has been caused by the expansion of other EU authorities, but also by the austerity reforms that enabled the EU to accept an additional 12 members since 2004. More on this matter can be found at: [http://europa.eu/pol/agr/index\\_en.htm](http://europa.eu/pol/agr/index_en.htm).

<sup>18</sup> European Council, Santa Maria da Feira, June 19–20, 2000: Presidency Conclusions, 16 (2000), in “Standardi Evropske Unije za državnu regulaciju poljoprivrede” (Standards of the EU for State Regulation of Agriculture), available at: <http://www.mreza-mira.net/wp-content/uploads/EU-standardi-za-regulaciju-poljoprivrede.pdf>

<sup>19</sup> Emil Erjavec and Dragi Dimitrievski, EU Common Agricultural Policy and Accession Tasks for Western Balkan's Countries, in *Western Balkan Agriculture and European Integration* 1, 2, available at: <http://www.agroedu.net/basic/publication/English.pdf#page=6>.

Despite a moderate advancement, the EU has assessed that the effort of BiH in CAP implementation is limited by poor coordination and implementation mechanisms.<sup>20</sup>

In order to facilitate the process of establishing funds, the EU provides support to countries on their path of European integration through the IPARD program<sup>21</sup> through the Framework, Sectoral, and Multiannual Financial Agreements. IPARD is a pre-accession program in place for the time period 2007–2013, and IPA 2 for the 2014–2020 period. They are part of IPA or, more specifically, its fifth component—Rural Development. The main aim of the IPARD program is to advance the agricultural sector through competitiveness of agricultural products, and its priorities are the following:

- Improving the market efficiency and the implementation of EU standards;
- Preparatory activities for the implementation of agro-environmental measures and LEADER (program that enables that projects are created and co-financed in certain regions or micro-regions, regardless of the existing administrative boundaries, which involve as many local interest groups as possible);
- Development of the rural economy.<sup>22</sup>

In order to commence with IPARD implementation,<sup>23</sup> BiH would have to sign the Sectoral Agreement with the European Commission and meet their conditions. The Sectoral Agreement states that the IPARD operative structure must consist of an administrative body and an IPARD agency. Furthermore, for access to the IPARD program, adoption of a rural development strategy is essential, as this strategy would represent the vision for the development of the entire country, with clear priorities and goals to ensure a uniform, just, and transparent development of the whole territory of the country. The strategy needs to be approved and accredited by the EU, and the State Certification Officer (SCO) bears full responsibility for

---

<sup>20</sup> Standardi Europske Unije za državnu regulaciju poljoprivrede” (Standards of the EU for State Regulation of Agriculture), available at: <http://www.mreza-mira.net/wp-content/uploads/EU-standardi-za-regulaciju-poljoprivrede.pdf>

<sup>21</sup> IPARD was founded on the basis of Council’s Directive number 1085/2006 and Commission’s Directive number 718/2007.

<sup>22</sup> More on this matter can be found at: <http://www.apprrr.hr/ipard-31.aspx>

<sup>23</sup> Under the assumption that the same principles of the legal framework for IPARD implementation would apply to the new financial framework of the EU for 2014-2020

the financial administration of EU funds in the beneficiary country and is responsible for the legality and regularity of all transactions.

The establishment of IPARD structures is important not only for the sake of access to IPARD funds, but also because such structures can be at hand when the state gains access to larger funds, the governing structure of which is identical to the IPARD structure. It should be noted that these are the funds that are given directly to farmers and rural communities that, with the help of these funds, would significantly contribute to the economic and social progress, the development of rural communities, and the raising of living standards in rural areas. BiH has still not established the requested IPARD structures and with further delays, farmers, citizens, and the whole country will suffer enormous economic losses.

## Analysis of Feasibility and Options

The research done by Green Council<sup>24</sup> has identified three policy options that can be taken into consideration for resolving the circumstances in agriculture and rural development in BiH. The research provided an overview of the advantages and disadvantages of their implementation.

Three options under consideration are the following:

- Maintaining the current state of the affairs—*status quo*;
- Establishment of a ministry of agriculture, food, and rural development of BiH;
- Strengthening of the institutional capacities of the Ministry of Foreign Trade and Economic Relations, i.e., the Sector for Agriculture, Food, Forestry, and Rural Development.

### ***Policy Option 1. Maintaining the Current State of Affairs—Status Quo***

After all that has been mentioned, it is clear that this policy option can in no way respond to the demands of the functional organization of the agricultural sector. In fact, this option is marked by constant delays in the European integration process, by failure to adopt essential reforms, poor coordination in the institutional system and, finally, enormous losses for farmers as well as for the entire economic development of BiH. Moreover, this situation has lasted for over a decade and the results are devastating both for the farmers and for the country.

---

<sup>24</sup> Ibid.

***Policy Option 2. Establishment of a Ministry of Agriculture, Food, and Rural Development of BiH***

This option would guarantee the most certain and permanent changes. Functional legal and institutional framework, which is in accord with the EU standards and the best practices and which involves a close cooperation of state and entity and lower institutions in the sector of agriculture and rural development would ensure uniformity of agricultural policy in the whole country and allow for a more efficient administration. One reference point at the state level would simplify the communication and prevent repetition of information between BiH and the EU.

The Ministry could be established either by changes in the constitution or upon approval by the entities.

The first approach may stabilize agricultural institutions and agencies more effectively than a mere legislation. For example, this approach may reduce the effects of future political conflicts over the agricultural and rural development sector and the implementation of the CAP. Furthermore, this sort of structure may aid in improving the process of decision-making and law enforcement.

The second approach—reaching an agreement between the entities—may provide a lower degree of stability than a constitutional reform would, because the entities might attempt to re-establish their own authorities or withdraw their agreement altogether.

***Policy Option 3: Strengthening of the Institutional Capacities of the Ministry of Foreign Trade and Economic Relations, i.e., the Sector for Agriculture, Food, Forestry, and Rural Development***

This option allows the entities to retain a considerable degree of authority over the agricultural policy and it cannot result in the same level of accord and efficiency as its alternatives would. This option cannot guarantee effectiveness in achieving the harmonization with the CAP or any other meaningful and permanent changes.

***Selection of a Policy Option***

After discussing the existing policy options, their advantages and disadvantages, we arrive at the conclusion that for a functionally administered agriculture and rural development sector, and the establishment of a system that will contribute to the effective development of this sector, providing

actual benefits for farmers and contributing to the general economic progress, the only real option is the establishment of a ministry for agriculture, food, and rural development of BiH. This option was also supported as the only real solution at the conference that took place in Sarajevo June 26, 2013, where the previous study by the Green Council was presented, titled “Establishment of the state-level ministry of agriculture, food, and rural development and other structures as a way of achieving economic progress for BiH in the EU integration process.”<sup>25</sup>

Through the cost-benefit analysis, the expenditures arising from this option will be identified and analyzed, as compared to monetized as well as non-quantifiable societal benefits of the establishment of a state ministry of agriculture, food and rural development.

## Financial Analysis

The aim of the financial analysis is the account of financial revenues. Two significant financial indicators taking into account the invested capital or public financial sources, are as follows:

1. Financial net present value (FNPV)
2. Financial internal rate of return (FIRR)

These financial indicators are calculated by discounting the cash flow, taking into account only cash inflow and outflow and not amortization, reserves etc., using the cash flow arising if the project is actually launched and not the existing one, which should be discounted for the sake of per-annum comparisons.

During the making of the cost-benefit analysis for the project of the establishment of a ministry of agriculture, food, and rural development of BiH, it seems appealing to define and select a specific time period. Nonetheless, we have chosen a six-year period (2015–2020), basing our decision on the period of availability of the IPA II funds (2014–2020). This is because within the economic analysis, as an important benefit, we will highlight the possibility of accessing the IPA II funds, as long as the requested IPARD structure is established at the state level (which will be enabled through the establishment of an adequate institutional and legal framework on the level of BiH).

---

<sup>25</sup> The list of persons who attended this conference is enclosed in Appendix 4

As the project in question is specific, not generating traditional revenues and, thus, there is no inflow, but the matter is rather of the investments and the expenditures of the establishment of a ministry of agriculture, food and rural development of BiH, in this part of the analysis we are going to focus solely on the cash outflow.

### ***Total Investments***

This concerns the investments into the fixed assets and project start-up expenses. Start-up expenses incur in the first monitored years, or rather upon the launch of the project, arising from the aim of creating adequate conditions for project implementation. Included into the calculations are the start-up expenses related to the staff recruitment and training, as well as consulting, notary, administrative, and other services. Since there is only the matter of investments and cash outflow, all these items have a negative value.

Investments into the fixed assets were calculated based on the indicators arising from the experience of establishing of other institutions on the BiH level. Investments into real estate were not calculated based on information, but on the already-established practice of accommodating institutions through rental of certain spaces, which is financed through operative expenses (rental of office spaces) that are calculated in the part of the analysis dealing with revenues and costs.

Investments into the equipment were calculated based on the empirical indicators and estimations, with the average amount of 10,000 BAM per employee. The investments have been carefully divided between the beginning two years of the project.

Start-up expenses were also calculated based on empirical data (based on the establishment of the Ministry of Defense BiH, and the establishment of the Food Safety Agency) and estimations of 500 BAM per employee for expenses of personnel recruitment, 1,000 BAM per employee for training costs and flat-rate estimated amounts for other start-up expenses. All start-up expenses have been distributed between the beginning three years of the project implementation, with the estimated dynamics of personnel recruitment in the first three years of the project (Ministry—150 new employees: 75+50+25, payment agency—100 new employees: 25+25+50). The estimation of the required number of employees in the Ministry and the Agency has been reached through conversations with the representatives of the institutions, experts in the sector, and by comparing practices

**Table 1. Overview of total investments into the project (BAM)**

Investment items	2015	2016	2017	2018	2019	2020
1. Real estate						
2. Equipment	-1,500,000	-1,000,000				
A. Total fixed assets (1+2)	-1,500,000	-1,000,000	0	0	0	0
1. Costs of staff recruitment	-50,000	-37,500	-37,500			
2. Staff training	-100,000	-75,000	-75,000			
3. Consulting, judiciary, notary, administrative and other services	-50,000					
4. Other start-up expenses	-100,000	-50,000	-30,000			
B. Total start-up expenses (1+2+3+4)	-300,000	-162,500	-142,500	0	0	0
Total investments (a+b)	-1,800,000	-1,162,500	-142,500	0	0	0

Source: Authors

from countries in the region with parameters that correspond to the BiH parameters.

Start-up expenses were not calculated for persons already employed in the state-level institutions and agencies, in charge of agriculture, food, and rural development (sectors in MoFTER BiH: Sector for Agriculture, Food, Forestry and Rural Development and the Sector for Natural Resources, Energy and Environmental Protection, State Veterinary Office of BiH, Administration of BiH for Plant Health Protection, Office for Harmonization and Coordination of Payment Systems in Agriculture, Food and Rural Development in BiH, Food and Rural Development and Food Safety Agency—in total 145 employees.)<sup>26</sup> The revenue analysis will also not include the existing costs of these administrative units at the state-level into its calculation. It is worth noting once again that only the expenses of newly employed personnel will be included into the calculations.

### *Operating Expenses and Revenues*

The operating expenses of the project projected in the cost-benefit analysis include all costs of operation with a character of a cash outflow. Therefore, these expenses do not include costs that do not result in cash outflow, such as amortization costs, which are, in fact, accounting costs that usually do not result in cash expenditures. Interest and taxation costs,

<sup>26</sup> Source: MoFTER BiH, 2011.

although resulting in cash expenditures, are not included in operating costs (interest costs are included in the financial analysis as a constituting part of a discount rate, while the taxation costs are only included in the project feasibility analysis).

Operating revenues do not include inflow due to state grants or value added tax. In order to establish the ministry in an adequate and functional way, means need to be secured for its functioning and financing of the operating costs of employee salaries and benefits, equipment and service expenses, as well as capital expenses.

Costs of employee salaries and benefits were calculated based on the mean gross salary and benefits of employees in the state-level ministries at the rate for 2015. Mean equipment costs per employee, as well as mean capital expenses per employee were projected based on the information on expenditures of the Food Safety Agency for 2015. All data was collected from the Draft Budget of the CoM BiH institutions for the time period 2014–2016.

State budget grants for operating a newly-established ministry were not calculated as cash revenues. Based on a set of interviews with representatives of institutions at different levels of governance, local, and international experts and civil society organizations, in relation to projections on functions of a future ministry and the number of new employees required for performing those functions, and on the basis of a comparative analysis of a number of employees in relevant ministries in Croatia and Macedonia and the analysis of potential transfer of employees of existing institutions on BiH level that are in charge of agriculture, food, and rural development, we have obtained a number of new employees needed to complement the existing structures and ensure efficiency and efficacy of all functions of the newly established ministry at the state level.

According to our analyses and projections, an additional 150 persons should be employed, so that they will, along with the existing personnel of state-level institutions, ensure an undisturbed, efficient, and effective performance of all designated functions of the new ministry of agriculture, food, and rural development, including the governing body within the requested IPARD structure (with all its duties and jurisdictions explained in the part of the document dealing with the contextual analysis of the project).

The dynamics of a complete systematization of the newly-established ministry and agency is as follows:

**Table 2. Overview of operating expenses and revenues (BAM)**

Items of operating expenses and revenues	2015	2016	2017	2018	2019	2020
1.						
A Total operating revenues (1+2+3)	0	0	0	0	0	0
1. Costs of employee salaries and benefits	-3,240,000	-5,670,000	-8,100,000	-8,100,000	-8,100,000	-8,100,000
2. Expenditures for equipment and services (energy, material costs, production services, etc.)	-1,560,000	-2,730,000	-3,900,000	-3,900,000	-3,900,000	-3,900,000
3. Capital expenses		-437,500	-625,000	-625,000	-625,000	-625,000
B Total operating expenses (1+2+3)	-4,800,000	-8,837,500	-12,625,000	-12,625,000	-12,625,000	-12,625,000
Net operating balance (a+b)	-4,800,000	-8,837,500	-12,625,000	-12,625,000	-12,625,000	-12,625,000

Source: Authors

- Ministry: 75 persons in the first year, 50 persons in the second year and 25 persons in the third year upon establishing.
- Agency: 25 persons in the first year, 25 persons in the second year and 50 persons in the third year upon establishing of the ministry.

All expense calculations refer only to the newly employed personnel, while the expenditures pertaining to the existing structures were not included in the cost-benefit analysis.

**Table 3. Overview of cash inflow and outflow (BAM)**

Cash flow	2015	2016	2017	2018	2019	2020	Total
1. Total operating revenues	0	0	0	0	0	0	0
A Total cash inflow (1)	0	0	0	0	0	0	0
2.1. Salaries and benefits	-3,240,000	-5,670,000	-8,100,000	-8,100,000	-8,100,000	-8,100,000	-41,310,000
2.2. Other expenses	-1,560,000	-3,167,500	-4,525,000	-4,525,000	-4,525,000	-4,525,000	-22,827,500
2. Total operating expenses	-4,800,000	-8,837,500	-12,625,000	-12,625,000	-12,625,000	-12,625,000	-64,137,500
3. Total investments	-1,800,000	-1,162,500	-142,500	0	0	0	-3,105,000
B Total cash outflow (2+3)	-6,600,000	-10,000,000	-12,767,500	-12,625,000	-12,625,000	-12,625,000	-67,242,500
Net cash flow (a+b)	-6,600,000	-10,000,000	-12,767,500	-12,625,000	-12,625,000	-12,625,000	-67,242,500
Discount factor	1,0000	1,050000	1,10250	1,15763	1,21551	1,27628	
Cash flow present value	-6,600,000	-9,523,810	-11,580,499	-10,905,903	-10,386,587	-9,892,030	-58,888,828
Discount rate	5%						
FNPV(C)	-58,888,828						

Source: Authors

As has already been noted, this project is not envisioned to lead to financial revenues and cash inflow, since it is aimed at establishing a ministry that is entirely to be financed from the state budget. Actual benefits for the economy and society are not discussed in the financial analysis, but rather in the part of the cost-benefit analysis that deals with the economic analysis of the project.

Salary expenses, operating material expenses and capital expenses rise gradually and in proportion to the systematization, therefore, the total operating expenses, after recruitment of personnel for the ministry and the agency are completed will reach the level of 12,625,000 BAM per year.

#### ***Cash Flow and Financial Net Present Value***

In part of the financial analysis that follows, the data from the previous two tables will be incorporated in the table that gives an overview of cash inflow and outflow pertaining to the project investments (*project cash flow*).

This table displays the estimations of the total cash outflow linked to the implementation of the project of establishment of the ministry of agriculture, food, and rural development, including the initial investments and all operative expenses. Operative expenses and cash inflow were not calculated and presented in the financial analysis.

As shown in the table, the total cash outflow for the project in the period between 2015 and 2020 would amount to 67,242,500 BAM.

Using the financial parameters of net cash flow, financial net present value (FNPV) was determined. FNPV was calculated using the recommended discount rate of 5 percent (the rate is recommended by the Euro-

**Table 4. Net discounted cash flow (BAM)**

<b>Year</b>	<b>Net cash flow</b>	<b>Cash flow present value</b>
2015	-6600000	
2016	-10000000	
2017	-12767500	
2018	-12625000	
2019	-12625000	
2020	-12625000	
<b>Total</b>	<b>-67,242,500,00 BAM</b>	<b>-58,888,894,67 BAM</b>

Source: Authors

pean Commission for the time period 2007–2013 for the purposes of financial analysis of investments). Net present value represents the worth of the invested cash in the future period in terms of its present-day value.

Discounting enables us to express, in present-day terms, the cash flow occurring in different time periods. Therefore, in present value, the total cash outflow of this project amounts to 58,888,894 BAM.

The financial rate of return (FRR), defined as a discount rate which reduces the financial net present value (FNPV) of the investment to zero value,<sup>27</sup> was not calculated for the project of establishment of the ministry of agriculture, food, and rural development, because of the obvious negative values of the net cash flow throughout the whole duration of the project, which is logical considering that we are analyzing a project without revenues or cash inflow in the traditional sense. The operative expenses of the ministry are financed from the budget and partially from the IPA funds, which in fact lessens the burden on the public sources of financing. Indicators of financial return (financial cost-efficiency of an investment) and financial sustainability are used to show if it is possible to compensate the total investments out of the net revenues. It is obvious that in projects of this sort it is not possible to compensate the total investments with the financial net revenues.

Only through economic analysis is it possible to demonstrate that the full economic and societal benefits arising from this project surpass the financial expenditures, which are unavoidable in the functioning of a public administration.

## Economic Analysis

The purpose of the financial analysis was to estimate the financial revenues that the project is supposed to yield. *The economic analysis identifies the benefits and losses for the overall society, which would arise from the project.*

As opposed to the financial analysis which relied on market values for calculations, for the purposes of the economic analysis book values (accounting values or shadow prices) are used. Book values take into account the social discount rate (SDR), which represents the minimum acceptable return from the whole society's point of view. SDR may differ

---

<sup>27</sup> Milan Čupić, "Cost-benefit analiza" (Cost-Benefit Analysis), Business Start-up centre Kragujevac, 2009.

from the financial discount rate due to market imperfections, however, for the purposes of the cost-benefit analysis we will adhere to the traditional principle that recommends that the social discount rate equal to the financial discount rate. In this analysis, we will use SDR of 5 percent.

In the process of economic analysis within the cost-benefit analysis, the following three steps will be undertaken:

1. Conversion of market to book values;
2. Inclusion and monetization of project's non-market (non-financial) benefits;
3. Discounting of estimated costs and benefits and calculation of indicators of project's economic return.

### ***Conversion of Market to Book Values***

When conducting an economic analysis, market values are converted to book values. Financial costs and benefits included in a cost-benefit analysis need to be expressed in socially acceptable values, meaning values that take into account the social discount rate (SDR).

In some projects—and the project of establishment of a state ministry of agriculture, food, and rural development is one of these projects—certain societal benefits account for the largest part of economic benefits, while financial benefits may represent a very small part of the total benefits. In such cases, it is not practical to make a conversion of financial to economic benefits and, therefore, in the creation of this cost-benefit analysis we will omit this step.

### ***Inclusion and Monetization of Project's Non-Market (Non-Financial) Benefits***

The next step in the economic analysis is the inclusion into the analysis the benefits of the project that are of social relevance and that need to be quantified and expressed in financial terms, or in other words subjected to the monetization process.

Based on a set of interviews with representatives of institutions at different level of governance, local and international experts and civil society organizations, and on the basis of own research, we have identified a number of economic benefits as well as benefits from the aspect of the whole society.

The text that follows brings only some of the consequences of the implementation of this project, which will finally provide considerable economic and social benefits:

1. Establishment at last of a requested IPARD structure that will allow for an efficient system of identification, formulation and application of IPARD program, monitoring and assessment of project implementation, promotion, reporting, coordination and implementation and payment functions;
2. Definition and implementation of adequate measures and activities for the export of our products to the demanding market of the European Union—increase in (re-establishment of) export of certain products to the markets of Croatia and the EU;
3. Definition and implementation of adequate measures and activities for regulating the import into BiH. The degree of import liberalization is unprecedented in the region, which is evident in the fact that within the CEFTA association only BiH has a nil custom rate for all products, while other countries hold agreed concessions for products that are of special interest for those countries;
4. Development of measures for stimulating local production;
5. Defining at last the agricultural policy and understanding the sector of agriculture and rural development as the strategic sector for the overall economy;
6. Equalizing the systems of agricultural subsidies and harmonizing them with the EU agricultural policy;
7. Establishment of a functional statistical support, which will allow for a timely and effective decision-making;
8. Direct effect on strengthening of the national security by strengthening the agricultural sector.

For the purposes of creating a CBA of establishing a state ministry of agriculture, food, and rural development, and in order to justify the need for implementation of this project, it is sufficient to quantify and monetize only the first two out of above-listed benefits. In relation to other listed benefits, the two selected benefits are relatively easy to monetize considering the availability of data from reliable sources.

Thus, we will monetize the benefits arising from the establishment of the IPARD structure and the benefits that would arise if conditions were met for an unhampered export of products of animal origin into Croatia,

which has been discontinued in July 2013 when Croatia entered the EU, due to the low degree of preparedness of local unsynchronized and uncoordinated institutions on all levels. Other benefits will be evaluated using a multi-criteria analysis, in order to confirm that the establishment of a state ministry is justified.

### **Benefit I: IPARD Structures and Funds— Monetization of Benefits**

The contextual analysis of this document provides basic information on IPARD program and the establishment of a requested IPARD structure. Using a comparison with Croatia, this part of the analysis will demonstrate the extent of loss of EU funds that BiH has experienced due to the absence of political will and the lack of synchronized and coordinated action for establishing the requested IPARD structure.

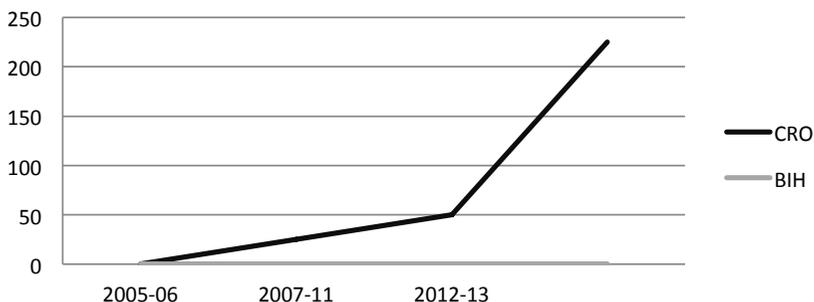
As the study conducted by the Green Council in the first half of 2013 has shown,<sup>28</sup> Croatia achieved a stable progress in the stabilization and accession process, by completing successfully all technical and political phases, including the closure of the negotiations of all 33 chapters of the accession agreement and since July 1, 2013 it has been a full member of the EU.

In the first 12 years since the start of the stabilization and accession process, Bosnia and Herzegovina has accomplished a progress equivalent to the progress that Croatia has made in the course of first 12 months. The implications of the low degree of progress toward achieving the mentioned objectives are not only political and technical. There are, more importantly, financial implications for every rural community, every farmer and every taxpayer in BiH. While Croatia took a number of difficult decisions in order to bring the benefits of the EU membership to its citizens, BiH made little to no progress.

Figure 4 displays the amounts of funds that have been paid to farmers and rural enterprises in Croatia since 2007, when the IPARD program came to effect.

---

<sup>28</sup> More on this matter can be found at: “Establishment of the state-level ministry of agriculture, food and rural development and other structures as a way of achieving economic progress for BiH in the EU integration process”, Green Council, 2013, available at: <http://green-council.org/publikacije>.

**Figure 4. Cumulative utilization of SAPARD & IPARD funds 2007–13**

Source: Green Council, 2013

The total investments planned for the whole duration of the IPARD program (2007–2013) amounted to over 300 million euros. This sum was to be paid directly to farmers and rural communities in Croatia. In addition, 25 million euros were allocated through SAPARD program during the period 2005–2006. It means that between 2005 and 2013, 325 million euros have been accessible to Croatian farmers and rural communities. At the same time EU funds were reserved but not at the disposal of their BiH counterparts. According to Eurostat data, there are 132,000 agricultural households (with over 1200 euros of production yearly), which means that the EU funds that have so far been available amount to a mean of 2.462 euros per household.

There is a simple relation between the chronology of the relations between Croatia and the EU and the funds at Croatia's disposal. The failure of BiH to make needed reforms and establish required state-level structures has prevented its access to funds from the IPARD program. In contrast, Croatia has since 2001 achieved a sufficient degree of progress to apply for access to IPARD funds in 2008 and ensure, thus, that funds aimed at farmers keep entering the country undisturbed since that moment on.

#### ***Overall Consequences of the Failure to Access IPARD Funds:***

Consequences of the current situation in regard to the stabilization and accession process and IPARD are as follows:

- While BiH farmers and rural communities have so far not able to access the IPARD funds, Croatian farmers have been given the equivalent of 2,462 euro per household;

- Funds that could have been at the disposal of farmers and rural communities in BiH were lost, re-absorbed into the EU budget, whether to be spent on other countries in the Western Balkans, such as Croatia, or elsewhere in the EU;
- Final beneficiaries have very little or no experience in the EU mechanisms of investment into agriculture and rural development and, accordingly, they do not understand its potential worth;
- Starting from already this year, Croatian farmers and rural communities have been enabled to access much larger funds. The funds will be allocated yearly to the farmers and rural communities in Croatia and they will grow exponentially;
- Until an agreement on IPARD structures is made, the inflow of funds will not be possible; farmers and rural communities will still be unable to access these funds that are aimed at improving the social and economic conditions they live in;
- The level of trust in the abilities of BiH institutions to reach an agreement in accord with the EU demands is low;

Through calculating the amount of funds in relation to the number of households in BiH, we obtained a projected amount of IPARD funds that could be available to BiH if required IPARD structures were established. Thus calculated financial inflow was foreseen as of starting from year 2018, considering that a period of at least three years is needed for accreditation of the payment agency.

Based on the calculations of data displayed in Table 5, the annual amount of IPARD funds that could be at disposal of BiH had the required IPARD structures been established, would amount to 78 million BAM and these means would have been available three years after the establishment of the ministry and the payment agency (upon accreditation). However, based on the interviews conducted with experts from relevant institutions and considering the slow-paced progress made by BiH on its way toward the European integrations and the absence of required degree of synchronization and coordination on all levels in the agricultural and rural development sector, we have been careful in our calculations to use the annual benefits from the IPARD funds in the amount of 30 million BAM. The implementation would be launched three years upon the establishment of the ministry and the payment agency (period of accreditation).

**Table 5. Monetization of Benefits I – IPARD funds (BAM)**

Estimated IPARD funds that could be available if the IPARD structure were established

Number of registered households in 2012*	IPARD funds, amount per household (€) <sup>a</sup>	Calculated amount of IPARD funds lost (€) <sup>b</sup>	Calculated amount of IPARD funds lost (bam) <sup>c</sup>
FBiH 48,509	2,462	119,429,158	232,886,858
RS 63,795	2,462	157,063,290	306,273,416
Brčko 2,436	2,462	5,997,432	11,694,992
Total for period 2007–13		282,489,880	550,855,266
IPARD funds—annual amount		40,355,697	78,693,609

Source: Authors

a. Number of households. Source: MoFTER's Report on Agriculture for 2012

b. Per-household amount of IPARD funds was provided based on the case of Croatia (2007–13)

c. Calculation of lost IPARD funds for a seven-year period, based on the analogy made with the funds utilized in Croatia

## **Benefit II: Export of Products of Animal Origin to Croatia After its Accession to the European Union—Monetization of Benefits**

Despite the importance of Croatia as partner in foreign trade and despite being timely informed on Croatia's accession to the EU, BiH was completely unprepared for this moment. Due to being late to adapt the legal framework and incapacitate the authorities to perform their duties, the state has potentially caused great losses for itself and its producers.

In the following text, we provide an overview of export of products of animal origin to Croatia in the period between July 2012 and March 2013 (prior to Croatia's accession to the EU) and between July 2013 and March 2014 (after Croatia's accession to the EU). It can be noted that the export to Croatia for the period after its accession to the EU (July 2013–March 2014) was lowered by 38,625,188 BAM than the exports done in the same time of the year prior to Croatia's accession to the EU (July 2012–March 2013). On the annual level, this loss amounts to 51,500,000 BAM.

After Croatia entered the EU, the annual loss in exports of animal origin products reached 51.5 million BAM. BiH's economy is too small to successfully overcome such large losses.

**Table 6. Overview of export of products of animal origin prior to the accession of the Croatia to the European Union (BAM)**

Export to Croatia from BiH 07-12/2012 01-03/2013 - products of animal origin		Export to Croatia 07-12/2012		Export to Croatia 01-03 2013		Export to Croatia 07 2012-03 2013		
TN	Tariff name	Quantity (kg)	Value (BAM)	Quantity (kg)	Value (BAM)	Quantity (kg)	Value (BAM)	
0105	Live domestic fowls			211	2,346.01	211	2,346.01	
0207	Fowl meat and edible slaughterhouse by-products	551259	2,491,256.23	20056	63,455.22	571315	2,554,711.45	
0210	Meat and edible slaughterhouse by-products	18054	277,993.51	3635	70,785.34	21689	348,768.85	
0301	Live fish	25620	142,431.33	8000	48,504.58	33620	190,935.91	
0302	Fish, fresh or cooled, except fish filets	144265	803,166.06	107629	651,067.65	251894	1,454,233.71	
0303	Frozen fish, except fish filets and other fish meats	61808	345,885.45	19884	92,525.80	81692	438,411.25	
0304	Fish filets and other fish meats	488	5,348.86	297	3,416.11	785	8,764.97	
0305	Dried, smoked and salted fish	180610	725,535.35	24109	108,815.77	204719	834,351.12	
0401	Milk and cream, non-concentrated and without sugar added	13154880	11,749,196.39	8163695	8,090,021.80	21318575	19,839,218.19	
0402	Milk and cream, concentrated or with sugar added	8074	21,403.95	303	804.97	8377	22,208.92	
0403	Buttermilk, sour milk, yoghurt, kefir	1079643	1,949,041.29	380838	722,346.21	1460481	2,671,387.50	
0404	Whey, concentrated or non-concentrated	10000	44,349.77			10000	44,349.77	
0405	Butter and other dairy fats	40187	283,273.18	15836	83,027.25	56023	366,300.43	
0406	Cheese and curd	556541	4,315,552.47	276587	2,148,495.70	833127	6,464,048.17	
0407	Bird and fowl eggs, fresh, shelled	893661	2,881,424.23	559143	1,924,210.63	1452804	4,805,634.86	
0408	Bird and fowl eggs, fresh, unshelled			8640	6,756.47	8640	6,756.47	
0508	Corals and similar materials, raw or minimally prepared	6	24.21			6	24.21	
0511	Other products of animal origin	1475020	14,423.99	817880	7,997.93	2292900	22,421.92	
	Total for 9 months:	18200115	26,050,296.27	10406742	14,024,577.44	28606857	40,074,873.71	
				Calculated annual export prior to Croatia's accession to the EU				53,433,164.95

Source: Foreign Trade Chamber of BiH

**Table 7. Overview of export of products of animal origin after the accession of the Croatia to the European Union (BAM)**

TN	Tariff name	Export to Croatia 07-12/2012		Export to Croatia 01-03 2013		Export to Croatia 07 2012-03 2013	
		Quantity (kg)	Value (BAM)	Quantity (kg)	Value (BAM)	Quantity (kg)	Value (BAM)
0105	Live domestic fowls						
0207	Fowl meat and edible slaughterhouse by-products						
0210	Meat and edible slaughterhouse by-products						
0301	Live fish						
0302	Fish, fresh or cooled, except fish filelets	105628	645,693.07	57220	355,115.78	162848	1,000,808.85
0303	Frozen fish, except fish filelets and other fish meats	53586	161,902.46	2040	12,368.66	55626	174,271.12
0304	Fish filelets and other fish meats	503	5,986.07	286	3,384.94	789	9,371.01
0305	Dried, smoked and salted fish	15434	111,613.08	20012	108,378.95	35446	219,992.03
0306	Crustaceans, with or without shells	522	10,301.82			522	10,301.82
0401	Milk and cream, non-concentrated and without sugar added	17	123.65			17	123.65
0402	Milk and cream, concentrated or with sugar added						
0403	Buttermilk, sour milk, yoghurt, kefir						
0404	Whey, concentrated or non-concentrated						
0405	Butter and other dairy fats						
0406	Cheese and curd						
0407	Bird and fowl eggs, fresh, shelled			11520	12,395.52	11520	12,395.52
0408	Bird and fowl eggs, fresh, unshelled						
0508	Corals and similar materials, raw or minimally prepared						
0511	Other products of animal origin	1475020	14,423.99	817880	7,997.93	2292900	22,421.92
	Total for 9 months:	1650710	950,044.14	908958	499,641.78	2559667	1,449,685.92
			Calculated annual export after Croatia's accession to the EU				1,932,914.56
			Revenue loss after Croatia's accession to the EU				51,500,250.39

Source: Foreign Trade Chamber of BiH.

### ***Discounting of estimated costs and benefits and calculation of indicators of project's economic returns***

Costs and benefits occurring in different time periods must be discounted to a present value. Unlike financial analyses where a financial discount rate is used, this economic analysis uses SDR - Social Discount Rate. The discounting procedure is the same as in a financial analysis, with the distinction that in the economic analysis, apart from the financial effects, identified economic and social non-market (non-financial) effects are also taken into account.

Indicators of project's economic return are:

- Economic Net Present Value (ENPV)
- Economic Rate of Return (ERR)
- B/C ratio (ratio between the present benefit value and the present value of the project costs)

The conditions of economic cost-efficiency are as follows:

$$\text{ENPV} > 0 \quad \text{ERR} > \text{SDR} \quad \text{B/C ratio} > 1$$

In order to state that a project is economically cost-efficient, it is necessary to confirm that the above-mentioned conditions are met. The economic net present value of the project must be higher than zero, the economic rate of return must be higher than the social discount rate (in this project this means it is higher than 5 percent) and the ratio of present benefit value to current cost value must be higher than 1.

As it has been demonstrated through the calculation of indicators of the project's economic returns (or revenues), all indicators confirm that the project is cost-efficient. The following graph compares the extent of the effects of the project, i.e., the extent of economic benefits in relation to the economic costs of the project.

Determined indicators of the project's economic return undoubtedly show that the project of establishing a ministry of agriculture, food, and rural development is a cost-efficient project.

### **Multi-Criteria Analysis**

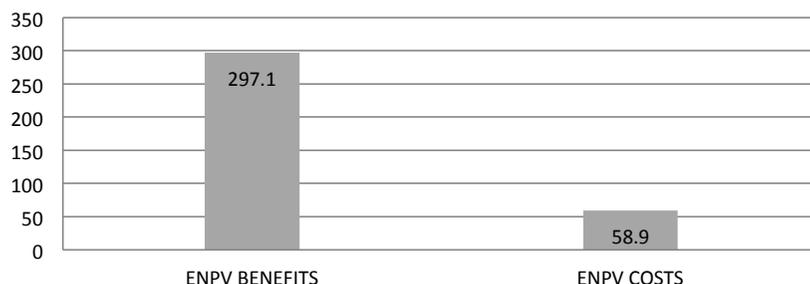
In the following economic analysis, we have monetized only the first two identified objectives: availability of IPARD funds and re-establishment

**Table 8. Economic flow of the project (BAM).**

Economic flows	2015	2016	2017	2018	2019	2020	Total
1. Total operative revenues	0	0	0	0	0	0	0
2. Benefit 1 - IPARD funds				30.000.000	30.000.000	30.000.000	90.000.000
3. Benefit 2 - Export to Croatia (products of animal origin)		51.500.250	51.500.250	51.500.250	51.500.250	51.500.250	257.501.250
A Total economic benefits (1+2+3)	0	51.500.250	51.500.250	81.500.250	81.500.250	81.500.250	347.501.252
2. Total operative expenses	-4.800.000	-8.837.500	-12.625.000	-12.625.000	-12.625.000	-12.625.000	-64.137.500
3. Total investments	-1.800.000	-1.162.500	-142.500	0	0	0	-3.105.000
B Total economic costs (2+3)	-6.600.000	-10.000.000	-12.767.500	-12.625.000	-12.625.000	-12.625.000	-67.242.500
Net economic effects (a+b)	-6.600.000	41.500.250	38.732.750	68.875.250	68.875.250	68.875.250	280.258.752
Discount factor	1,0000	1,05000	1,10250	1,15763	1,21551	1,27628	
Economic net present value	-6.600.000	39.524.048	35.131.746	59.496.774	56.663.664	53.965.627	238.182.225
Economic benefit present value			297.071.120				
Economic cost present value			-58.888.895				
Economic net present value			238.182.225				
Indicators of project's economic returns							
SDR	5%						
ENPV	238.182.225		ENPV>0				
ERR	6,32		ERR>SDR				
B/C ratio	5,04		B/C>1				

Source: authors.

**Figure 5. Relation between economic benefits and costs of establishment of the ministry of agriculture, food and rural development of BiH (million BAM).**



Source: Authors.

of export to Croatia of certain agricultural products the export of which has been suspended by Croatia's accession to the EU.

Other identified objectives and outcomes or potential benefits are not easily monetized without a good statistical database and a study of a longer duration. In order to evaluate the influence of other outcomes of this project, we conducted multi-criteria analysis (MCA), which indicates which of the three defined options results in the best outcomes in relation to the objectives and benefits we have previously identified and formulated.

The first step in the multi-criteria analysis is formulation of options to be assessed (this has been done in Section 4. Analysis of feasibility and

**Table 9. MCA criteria and evaluation of their importance**

Criterion	Criterion value	Ponder
IPARD / structure establishment /availability of funds	50	0.11
Export to the EU and other demanding markets	80	0.18
Establishment of functional statistical support that will allow for timely and effective decision-making	40	0.09
Coordination and synchronization of subsidies for agriculture / protection and stimulation of local production	70	0.16
Political support and feasibility of the option	100	0.23
Increase in the level of national security	100	0.23
Total	440	1.00

Source: Authors.

options), as well as criteria on the basis of which the evaluation of given options is to be done. The identified and formulated criteria are evaluated in relation to the total outcome of the multi-criteria analysis.

As displayed in Table 9, the greatest weight was assigned to the increase in the level of national security and the political support and feasibility of the option, followed by the export to the EU and other demanding market, considering that the increase in production and export directly influences the rate of economic growth. In the next step, we assess all options based on individual criteria.

The option to establish the state ministry of agriculture, food, and rural development was assessed the most effective based on all criteria—which has already been confirmed in the analyses above (contextual analysis, analysis of feasibility and options, financial and economic analysis)—except based on the criterion “Political support and option feasibility,” where Option I—maintaining the current state of the affairs—has been assessed as most certain.

In order to reach the outcome that brings the highest benefits in mathematical terms, we multiplied the values that these options achieved for each criteria.

The results of the multi-criteria analysis correspond to the results of the CBA: based on almost all criteria, the option for establishing a state ministry of agriculture, food, and rural development has been assessed as the option that will yield the greatest economic and social benefits.

**Table 10. Assessment of options based on each MCA criterion**

<b>Criterion</b>	<b>Option I Maintaining the current state of affairs</b>	<b>Option II Strengthening of the Sector in MoFTER</b>	<b>Option III State ministry</b>
IPARD funds	0	100	50
Export to the EU	10	80	50
Statistical support / efficient decision-making	20	80	50
Protection of local production / synchronization of subsidies	20	80	40
Political support / option feasibility	100	20	80
National security	20	80	40

Source: authors.

**Table 11. MCA: Pondered assessment of given options.**

Criterion	Option I	Option II	Option III
	Maintaining the current state of affairs	Strengthening of the Sector in MoFTER	State ministry
IPARD funds	0	100	50
EIPARD funds	0	11	6
Export to the EU	2	15	9
Statistical support / efficient decision-making	2	7	5
Protection of local production / synchronization of subsidies	3	13	6
Political support / option feasibility	23	5	18
National security	5	18	9
Total	34	69	53

Source: authors.

## Risk Assessment

When conducting a financial and economic analysis of a project, there is always a possibility that the author failed to evaluate all parameters. That is why project risk assessment is always added to the analysis.

Risk assessment is based on the analysis of a probability that the project will indeed result in desired effects. This probability ranges between 0 and 1, where 0 represents a certainty that project will not yield these effects and 1 represents a certainty that the project will result in these effects, while all values between 0 and 1 represent a certain degree of probability (rather than certainty) of these effects.

In the continuation of the risk assessment part of the CBA, we conducted a sensitivity analysis (the identification of the project's critical factors and quantitative analysis of the effects of critical factors on the project).

## Sensitivity analysis

The sensitivity analysis identifies the project's critical factors. As a general rule, factors are critical when a change in their estimated value by 1 percent causes a change in project's net present value (NPV) by more than 1 percent.

**Table 12. Identification of critical factors**

Category	Possible factors
Total investments	Inflation rate, change in prices of products and services, reduction in sources of financing, failure to meet deadlines, etc.
Operative expenses	Inflation rate, change in prices of products and services, change in labour wages, change in energy prices, etc.
Benefit I – IPARD funds	Political instability, inadequate projects, decrease in funds, etc.
Benefit II – Export to Croatia (products of animal origin)	Change in production rate, political instability, lack of coordination and -preparedness for changes, etc.

Source: Authors

Provided below is an overview of identified critical factors for this project.

After we identified the critical factors, we performed a quantitative analysis of the effect of factors on project's economic net present value (ENPV):

As it is clear from the table, none of the critical factors affect the project impacts significantly. With the change of the value of identified factors by 1 percent, the NPV does not change by more than 1 percent.

Risk assessment, i.e., a sensitivity analysis and a quantitative analysis of potential critical factors, determined that none of the identified factors is of a significant risk for the impacts of the project of establishment of a ministry for agriculture, food, and rural development.

## Recommendations

The solution to the problem of general discord and lack of coordination in the implementation of an agricultural policy, as well as to the stagnation in the sector of agriculture and rural development in BiH, should certainly be sought in the strengthening of institutional organizations and jurisdictions at the state level. Keeping in mind everything that has previously been stated, the recommendations for advancement of the agricultural and rural development sector are the following:

- Establish a unique ministry of agriculture, food, and rural development of BiH with the authority to create, develop, and coordinate

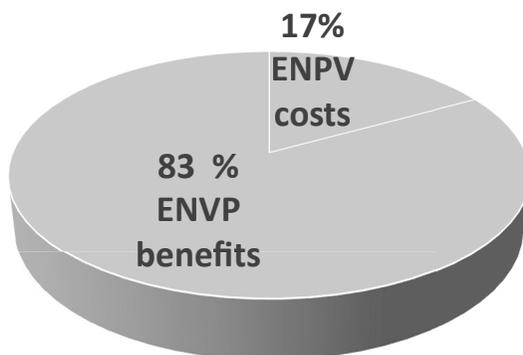
**Table 13. Quantitative analysis of the effect of factors on the ENPV.**

Factor	Percentage of change in factor	Percentage of change in ENPV
Total investments	+2%	-0.025 %
	+1%	-0.013 %
	-1%	+0.013 %
	-2%	+0.025 %
Operative expenses	+2%	-0.469%
	+1%	-0.234 %
	-1%	+0.234 %
	-2%	+0.469 %
Benefit I – IPARD funds	+2%	+0.622 %
	+1%	+0.311 %
	-1%	-0.311 %
	-2%	-0.622 %
Benefit II – Export to Croatia (products of animal origin)	+2%	+1.872 %
	+1%	+0.936 %
	-1%	-0.936 %
	-2%	-1.872 %

Source: Authors

agrarian/agricultural policies and to set strategic goals for agriculture and rural development of BiH, to create measures of structural agricultural policies, market and prices, customs and foreign trade, land, taxes, and measures of support for agriculture in accordance with standards of the EU, as well as other agreed authorities in relation to agriculture, veterinary sector, plant protection, food safety, forestry, water management, and rural development;

- Urgently create a strategy of rural development for BiH, as a priority and a condition of future access to the IPA 2 program;
- Urgently make a decision on forming the required IPARD structures, including the governing body within the ministry and IPARD payment agency on the state level;
- Support the work of the Office for Harmonization and Coordination of Payment Systems in Agriculture, Food and Rural Development in BiH by putting it into a full function with planned capacities and overtaking its function as a future IPARD payment agency.

**Figure 6. Current value of benefits and costs (in million euros)**

- Implement the remaining activities defined by the “Action Plan for Mitigation of Consequences of Croatia’s Accession to the European Union” so that the export to Croatia could be accelerated.
- Strengthen advisory offices so that they have capacities to offer quality services in preparing and writing of project proposals for IPARD funds for all farmers and rural communities in BiH

## Conclusion

Bosnia and Herzegovina is an underdeveloped state that does not recognize the agricultural and rural development as strategically crucial for the development of the entire BiH economy. Too much time and too many funds were lost over superficial changes in this socio-economically important sector, without concrete and visible results. It is essential that decision-makers implement the recommendations given in the Resolution on the progress of BiH in the European integration process, adopted by the EU on February 6, 2014. This Resolution points to the urgent establishment of a ministry of agriculture, food, and rural development of BiH.

For the purposes of this analysis, a CBA was done for two out of eight listed benefits (that would be the result of the establishment of the IPARD structure and as a consequence of meeting the conditions for an unhampered export of products of animal origins into Croatia or the EU). Even so, the two analyzed benefits greatly outweigh the cost indicators, and they represent enormous benefits that BiH and its farmers and rural communities may achieve if a functional ministry is established. Figure 6 dis-

plays the relation between the costs and benefits, additionally supporting the arguments for establishing a ministry of agriculture, food, and rural development for BiH.

After comparing the costs and benefits pertaining to the establishment and operations of a functional ministry of agriculture, food, and rural development, we can conclude that, based on almost all criteria, this is an option that can result in the largest economic and social benefits.

As this cost-benefit analysis has demonstrated, only the establishment of a ministry for the sector of agriculture and rural development can guarantee permanent changes and enable quality planning and development, contributing to economic and other benefits for Bosnia and Herzegovina and its society.



## *Chapter 5*

# **Reforms in the Banking Sector**

*Edin Karabeg*

This article does not aim to focus on banking in Bosnia and Herzegovina (BiH), although it will provide the reader with a short insight into the country's banking sector. We do not claim that the topics mentioned are complete or all-encompassing, but they are intended to provide the reader with a brief overview of important issues of the economic everyday life in BiH, as well as offer incentives for possible solutions to common issues. This paper focuses on certain burning aspects of the economy of BiH which, of course, tackle the banking sector as well. We mention some of the needed reforms that should be introduced as soon as possible to prepare the Bosnian economy for possible European Union (EU) candidate status, and make it a competitive environment for future investments. There are many ways to approach this topic, from various stand-points—economic, political, or legal. However, the views expressed here stem mainly from the author's work as a banker, and from a general financial point of view. Of course, some of the points are closely linked to the other two standing points, especially those related to tax provisions and the rule of law, as both have an impact on daily banking operations. Nevertheless, banking is one of the most stable industry sectors in BiH, despite experiencing stagnation during the last few years.

Looking briefly into the recently published macroeconomic indicators of BiH, one can get the impression that the country is recovering, albeit slowly, from the crisis and its aftermath in the years 2008–2010. Since 2012, GDP showed a steady growth between 1.5 percent and 3 percent—interrupted only by the huge floods in 2013, where growth in BiH turned negative due to the destructive effects for its people, the economy and the environment. In their outlook for 2016 and the years following, analysts foresee a GDP growth of 3 percent and above for the region.

However, if we take a deeper look, we will recognize very quickly that the economic situation is quite unsustainable. BiH is in the midst of a second-crisis phase. The country has a stable financial environment, international banking groups have been present in the country for years, and

many projects in the areas of infrastructure, tourism, and energy exist; yet substantial domestic and foreign investments are still missing.

## The Banking Sector in Bosnia and Herzegovina

Bosnia and Herzegovina's banking sector is stable (although less attractive than it used to be before 2008). Foreign funds are flowing into the country, seeking opportunities for quick profits. This is not unreasonable—and would be expected if the economy would boom. Local authorities have very well recognized that a strongly present Central Bank is crucial for the country's survival.

The economy is underpinned by a convertible currency with fixed parity to the Euro. As a result, the convertible mark is one of the most stable currencies in Southeast Europe. The banking sector in Bosnia and Herzegovina remains reasonably liquid and well capitalized. Foreign banks account for over 90 percent of total assets in the financial system, but the banking sector has not been subject to large credit outflows to parent banks.<sup>1</sup>

A total of 25 banks exist in BiH, where 17 have their headquarters in the Federation of Bosnia and Herzegovina (FBiH), and eight in Republika Srpska (RS). As calculated at the end of June 2016, their total assets amount for around 25 billion BAM, whereas their total capital accounts for around 3.5 billion BAM.<sup>2</sup> We can thus conclude that around 95 percent of their total assets are non-domestic.

The number of banks seems to be in reasonable proportion to the size of the market. However, two foreign capital banking groups dominate with a market share of around 50 percent, i.e. UniCredit Group (Italy) and Raiffeisenbank (Austria). Aside from these two, the biggest groups operating in BiH are Intesa San Paolo (Italy), Sberbank (Russia), Erste Group (Austria), NLB (Slovenia) and Nova Banka (a domestic bank). The American hedge fund *Advent* recently entered the market by purchasing the larger part of former Austrian bank Hypo Alpe Adria International.

<sup>1</sup> "Overseas Business Risk—Bosnia and Herzegovina." Foreign and Commonwealth Office, U.K. government. August 21, 2017. <https://www.gov.uk/government/publications/overseas-business-risk-bosnia-and-herzegovina/overseas-business-risk-bosnia-and-herzegovina>.

<sup>2</sup> All data used here are from the Central Bank of Bosnia-Herzegovina (<http://www.cbbh.ba>) or from the banking agencies of the country, <http://www.fba.ba>, <http://www.abrs.ba>.

In the first half of 2016, the total banking sector earned a total of 171 million BAM, which represents a return on equity of roughly five percent. The two largest banking groups showed a profit of above 100 million BAM in the first six months of 2016. The total exposure of Bosnian banks amounted to 16.97 billion BAM, of which households counted for 7.95 billion BAM by the end of August 2016. At the same time, the volume of deposits corresponded to 17.2 billion BAM, of which 10.2 billion BAM stemmed from the retail sector. What is important to mention is the fact that both key loans categories (retail and corporate) registered positive growth rates, but the growth of corporate loans outpaced that of retail loans for the first time since July 2013. Compared to the same period in 2015, corporate loans showed a growth of 3.6 percent, up to 7.97 billion BAM (46.8 percent of total loans) while retail loans saw an increase of 2.2 percent, reaching a value of 7.93 billion BAM, or 46.6 percent of total loans. The level ratio of non-performing loans (NPLs) at the end of June equaled 12.1 percent, and continued a downward trend after it reached its peak in Q3 2014.

All this data mirrors the general economic situation in the country. A country where the average monthly net salary stands at 830 BAM, the GDP per capita is 4,800 dollars, and the trade deficit reaches a level of above 40 percent. In such an environment, it is difficult for banks to achieve returns of 15 percent and above like in other developing regions.

Furthermore, recently, we have seen a record high in banks deposits. This should not be viewed as the result of increased wealth, but it is rather shows the lack of confidence in the country's economic prospects. Following this development and the bankruptcy of two small local banks, the Central Bank responded by increasing the mandatory reserve requirement, which additionally decreased the available amount of money for lending, and increased costs. Two banking agencies exist in BiH, one for each entity, which forces many banking groups to establish two banks in the country. Due to political reasons, it is not possible to merge the banks, which causes inefficiency, additionally increasing the costs of capital and decreasing potential returns. All this might be why at present no serious international banking group is interested in entering the local market.

The risk entry level for lending in the country is very low compared to Western Europe. For cash loans in retail lending it is common that one receives tenures of 12-15 years (sometimes even more), with interest rates between 4.5 percent and 8.5 percent. Households often cannot afford

shorter payback periods and prices of goods, especially of those imported, to equal the prices in the West.

Corporate lending refers only to basic instruments; the hedging of Foreign Exchange (FX) risks or interest risks is hardly seen on the market, and even the governments (both at the federal and entity levels) do not use such hedging instruments for their loans from international organizations such as the EBRD, EIB, or the IMF. As most of these government loans are given on a long-term basis (20 years and above), many of them have grace periods. Consequently, the government does not pay back the annuities for few of them, not realizing that it takes over a liability that will burden the next generation. By not hedging these obligations, it seriously jeopardizes its future development.

In general, corporate balance sheets are characterized by very low profit before tax as a result of the existing habit of tax avoidance. Although the government introduced a flat tax rate of 10 percent, the tax behavior of entrepreneurs did not improve significantly. There are several reasons for this, one of them being that the government and state owned companies are the biggest tax evaders. The other reason is based on an inefficient tax authority. We will elaborate on this later.

The attractiveness of doing business in Bosnia and Herzegovina is limited. On the one hand, there is a low domestic demand for goods, and on the other, many of the valid laws in the country were established in the former communist Yugoslavia, which are obstacles in times of free economies and the freedom of moving goods and money. The total number of corporations, and small and medium sized enterprises (SMEs), amount to 24,147, whereas the number of small business totals 46,631.<sup>3</sup> The overall number employed was approx. 489,600. When we look at a country similar in size, Austria has approximately 435,631 SMEs.<sup>4</sup>

A further problem in Bosnia and Herzegovina is the high administrative burden, especially for start-up companies. On the World Bank's ranking for ease of starting a business, BiH stands at 175 in the ranking of 189 economies.<sup>5</sup> The notary system was introduced in 2007, bringing

<sup>3</sup> This data is from 2014.

<sup>4</sup> Austrian Ministry for Finance (2011): [https://www.bmf.gv.at/.../Unternehmen\\_Anzahl\\_OE-NACE\\_4Steller\\_20121107.xlsx](https://www.bmf.gv.at/.../Unternehmen_Anzahl_OE-NACE_4Steller_20121107.xlsx)

<sup>5</sup> Worldbank, Doing Business 2016: Bosnia and Herzegovina, <http://documents.worldbank.org/curated/en/659921467991987957/pdf/100666-WP-Box393240B-PUBLIC-DB2016-BIH.pdf>

a lot of security into the corporate business. However, the country is far away from a “one-stop-shop,” where all formalities are handled in one stop. It takes anywhere from two weeks to two months to register a new company and to receive all the necessary approvals. Furthermore, start-ups face difficulties to organize capital—banks generally do not support them with lending due to the high rate of dropouts. Certain municipalities in BiH started programs supporting start-ups (mainly to fight unemployment). These programs either support interest payments, or even provide limited capital to start-ups. However, these initiatives are not centrally coordinated on the state or entity levels (e.g., by the Ministry for Economy and Development), but are actions set by individual cantons or municipalities and are generally very modest in their contributions.

Based on what is stated above, it is not easy for banks to earn money. As mentioned before, the barriers for retail lending are very low compared to other markets in the region. In corporate business, the fierce competition is leading to historical lows in interest lending. Dozens of subsidiaries in the Bosnian market are able borrow money cheaper than their parent companies in other countries. There are cases where parent companies are borrowing money from Bosnian banks through their subsidiaries. The calculation for such low interest rates is simple: banks hope that they can make up for the low margins by getting employees and the side businesses of these companies. Nevertheless, such an approach carries certain risks, especially if rates start to grow with higher traffic. Such a scenario might be difficult to imagine given the current environment, but looking at the rate history—everything is possible.

### **How Do Banks Earn Money in Bosnia and Herzegovina?**

Banks in BiH mainly earn their money through retail banking. And thus, only an extensive number of clients can allow banks to be profitable. Despite the fact that loan amounts are small and payback periods are extremely long for cash loans (the payback period for mortgage loans ranges from 15 to 30 years), the offered products are very simple. Most international banks simply roll-out their simplified product portfolio from their home markets onto the Bosnian market. Therefore, retail business consists largely of lending, savings, simple card business and additional electronic and mobile banking.

The lending business is limited to ordinary repayments. Hedge instruments are not offered because most people taking out a loan cannot afford to buy any derivatives. A couple of years ago a very small number of banks offered loans in Swiss currency (CHF), inviting borrowers to take advantage of the low Swiss LIBOR. However, as none of the loans was hedged against FX risk, this “adventure” ended in a disaster that resulted in extremely high non-performing rates when the Swiss Franc gained to the Euro. It became a political discussion as well, where local politicians accused banks of robbing people. This discussion is still ongoing in BiH, albeit with lower density. A law was passed prohibiting banks to offer loans in other currencies exempt in the Bosnian Mark (BAM) and the Euro.

The savings business consists of various interests given based on the tenor of the deposit. CDs (certificates of deposits) were not implemented in the Bosnian market until recently. As their use requires significant administrative effort to acquire all necessary licenses, they are not commonly used in the market. In general, certificates or bonds are not used as a way of saving in BiH, neither for companies or for households. Interest rates for deposits are extremely low, which further deteriorates the banks’ reputation in the eyes of private individuals. Nevertheless, savings have outpaced the growth of loans for several years, and the trend of replacing foreign funding of banks with local deposits continues. The problem of those deposits is their maturity structure. The low interest rates on deposit savings leads to an increase of over-night deposits, consequently leading to a miss-match of banking liquidity maturities. Approximately 25 percent of all deposits are overnight deposits in BiH.

The card business is also mainly focused on extending payback periods as much as possible. Therefore, banks introduced the so-called shopping cards a few years ago, which enjoy great popularity among cardholders. Shopping cards are established through arrangements between banks and retailers, which enabled banks to offer interest free deferred payments to their clients, while the retailer pays the interest directly to the bank. On the other hand, real loyalty programs hardly exist in the local market. One reason is that such programs require high levels of investment by participating partners, which is often not profitable. Another reason is the low purchasing power of clients, so that companies prefer to establish their own loyalty programs—without the involvement of banks.

There is still no law on electronic signatures in BiH, and the paper-based administration causes additional burdens for banks. All public correspondence is printed and signed manually, and those papers are stored

for many years. Simple operations such as opening a bank account cannot be performed online but must be done in person. The law does not foresee another way of identifying except the personal show up to the branch. Local authorities, to protect the rights of the clients, have issued many new laws and regulations in the past few years. However, the result is that you get roughly 40 pages of printouts to open an account, which you have to sign. So just an account opening requires in total 80 pages of printouts, one copy for the client and one copy for the bank. It is a similar procedure for all other products. Only the paper work load creates a lot of costs for banks, if only for the required safe storage of all these documents.

Accessibility to online banking in is very low compared to Western European countries, and so branches are the backbone of retail business in Bosnia and Herzegovina. Therefore, banks rely heavily on their branches, and it is thus not a coincidence that the two biggest banks also have the largest branch networks. According to the Bosnian Regulatory Agency for Communication, there were 636,725 online banking users by the end of May 2016, which amounts for 17 percent of the total population.<sup>6</sup> At the same time, the Agency estimates that 2.8 million inhabitants are frequent users of the internet. The Central Bank of Bosnia and Herzegovina reports that at the same time there are 2,013,219 cardholders and 314,777 subjects using some sort of internet or mobile banking. We can thus conclude that only 16 percent of cardholders are active users of online services provided by the local banks. New trends in retail banking to reduce local branches and instead attract people to complete transactions online have not been successful as of yet. Currently, there are attempts for branches to operate with automated machines, but until now it is difficult to predict if this is a sustainable way of doing banking business in BiH in the future.

The two biggest banks on the market serve between 600,000 and 1,000,000 clients today. Smaller banks have between 100,000 and 150,000 clients. Due to their smaller market shares, the costs of enlarging their domestic operations are very high. Additionally, customer readiness to change banks is extremely low, and employer often persuade their employees to open accounts with banks they are already doing business with. It is easier for the employer to complete payroll transactions with banks they have worked with in the past, and sometimes the company receives better

---

<sup>6</sup> Bosnian Regulatory Agency for Communication.

conditions when many of its employees have their salary account with the same bank.

Aside from the fact that the market is small and salaries are low, the margins in retail banking are better than those in surrounding countries. Through modernizing the law on day-to-day business operations, establishing less interference on the freedom of business, and especially by incentivizing capital injections into the country (primarily FDI—not considering banks), BiH could become a more interesting strategic area.

## **Drastic Changes are Needed**

There is a sense that the general public in BiH has become accustomed to the present economic situation—which is not true. The country has been avoiding desperately needed reforms for a long time, in particular those related to the economy and the rule of law. Such reforms are a prerequisite for creating a business climate that will attract international and domestic investment. Last year, the European Commission summarized the current status of required reforms in BiH:

The consensus on economic policy essentials has increased. A broad agreement has been reached on economic reforms, but the government now needs to show strong reform commitment by starting to implement the planned reforms. The consensus between the authorities at different levels of government on the economic policy essentials has broadly gained momentum with the adoption of the global framework for fiscal policies and balances 2016–2018 by the Fiscal Council.

In February 2015, Bosnia and Herzegovina submitted its Economic Reform Program covering the 2015–2017 periods. The program sets out an overly ambitious fiscal strategy based on reductions in expenditure but lacks initiatives that would stimulate growth. In addition, although some major obstacles for growth were identified, the structural reform strategy is vague on medium-term measures beyond 2015. There is ample room for improvement in terms of policy coordination. Following the adoption of the Reform Agenda in July, Bosnia and Herzegovina is encouraged to take further steps towards its implementation, including with the help of the ERP recommendations set out below, which reflect Reform Agenda priorities

The IMF Stand-By Arrangement (SBA), agreed in 2012, expired on 30 June 2015 but the last loan tranche disbursement was made in July 2014. The program went off-track due to delays in implementation of previously agreed structural reforms. Negotiations for a new IMF program have been ongoing.<sup>7</sup>

In September 2012, the IMF approved a three-year 405.3 million euros Stand-By Arrangement (SBA) to support the country's structural reforms envisioned in the 2012–2014 economic program, with a focus on reforms aimed at improving national policy coordination, advancing fiscal consolidation and public sector reforms, safeguarding financial sector stability as well as supporting growth and job creation through structural reforms. After this disbursement, BiH did not fulfill the necessary benchmarks, which resulted in delays for the remaining tranches.<sup>8</sup> This year, since additional funding was necessary, a newly extended fund facility in the amount of 500 million euros was agreed on to support these structural reforms.

However, instead of introducing changes, modernizing the financial and fiscal systems, BiH's institutions do not show the courage and resilience to introduce such steps, which would significantly decrease bureaucratic red tape and increase efficiency. As a result, we are faced today with an inefficient tax system, weak legal security, old (originating from Yugoslav communist times) employment laws, and a high current account deficit. Even the movement of people and the mobility of the labor force remain a concern: "the absence of harmonization in employment and labor legislation, of rights based on employment (i.e., health, pension, social and unemployment insurance) and other related taxation issues effectively prevent mobility inside the country."<sup>9</sup>

One of the key topics is the education system. During the times of the former Yugoslavia, the universities were highly respected, with professors who were often internationally educated and enjoyed an excellent reputation. After the Dayton Peace Agreement, the university system became regulated on the Canton level in the Federation of Bosnia and Herzegovina (FBiH). As a result, a lot of new universities have been opened (in both

---

<sup>7</sup> European Commission, Commission Staff Working Document, Bosnia and Herzegovina 2015, Brussels, November 10, 2015, p.30

<sup>8</sup> "Overseas Business Risk—Bosnia and Herzegovina." Foreign and Commonwealth Office, U.K government. August 21, 2017.

<sup>9</sup> European Commission, Commission Staff Working Document, Bosnia and Herzegovina 2015, Brussels, November 10, 2015, p.39

Republika Srpska (RS) and FBiH)—sometimes with a questionable standing. Unfortunately, many of them prioritized the business side over the education itself. At the same time, public universities struggle with budget issues as the government cannot afford to spend more on education. The graduates from private universities are often “very far from the economic reality,” which results in high unemployment. Therefore, parents who can afford it, often send their children abroad to complete their education. Once they graduate, they rarely return to BiH, as they find high-paying jobs in other countries. Based on this, the European Commission recommended in their Economic Reform Programs (ERPs) to “develop a more strategic approach to tackle the deficiencies in the training and education system by effectively prioritizing measures based on a mapping of the skills gap taking into account the needs of industry, especially SMEs. Harmonize legislation and standards related to education and training at state and entity level, as well as at cantonal level, since the competence on education in the Federation is at cantonal level.”<sup>10</sup>

Considering this, the government needs to introduce more changes to the existing labor laws. Labor laws in both entities need to be modernized and harmonized with each other. Despite the fact that FBiH adopted a revised labor law last year in July, which was met with trade union protests, the employers are still put in an inferior position. The fact that employees who have an unlimited contract cannot be laid off, this automatically leads to lower overall employment. Another result of the existing labor laws is that many unprofitable public companies cannot be revitalized as they keep the number of “employed staff” too high. This measure has a social connotation, but many of these companies pay delayed salaries and/or do not pay the social obligations for their staff to the government at all. The employment rate in the country is around 44 percent, and unemployment among young people (15–24 years old) was at 63 percent in 2014. To make matters worse, more than 80 percent remain long-term unemployed (i.e., unemployed for one year or more).<sup>11</sup> Therefore, the European Commission recommended that “labor market rigidities have to be reduced by addressing disincentives to hiring, including taking further steps towards a reduction of the tax wedge while ensuring budget neutrality.”<sup>12</sup>

---

<sup>10</sup> *Ibid.*, p.35

<sup>11</sup> *Ibid.*, p. 45

<sup>12</sup> *Ibid.*, p. 31

Linked to this topic is the fact that BiH shows a limited private wealth creation. This is partially based on a disproportional large public sector that has only partially been reformed since Yugoslav times. State owned enterprises provided large-scale employment in former communist times, yet most of these companies do not have the same market access they had before the war. Nevertheless, the maintenance of employment in these state-owned enterprises represents the main focus in order to keep social peace in the country. However, the high costs for these companies are eventually paid by taxpayers. In return, this creates a negative spiral and bias against employment.<sup>13</sup>

The development of significant foreign investments could increase the attractiveness of the private sector for young people entering the job market. Still, the majority of young graduates prefer to work for the public sector, which remains the largest employer (32 percent). This inevitably leads to economic ruin over the long term.

A move towards the liberalization of the labor law would cause a social problem in the short-term. Therefore, such changes would need to be accompanied with social solutions for a part of the population. Nevertheless, it is crucial to solve the topic as soon as possible, as postponing would have much larger negative impacts on the economy and social freedom in the future. Generally, the implementation of the legislative framework on social protection remains low. In both entities, due to financial constraints, the government did not implement social benefits prescribed by social protection laws, which include benefits not being paid, or amounts reduced according to available funding.<sup>14</sup>

## **The Fight for Capital**

Bosnia and Herzegovina and its authorities have to recognize that the whole region is competing for capital. In our globalized world, the attractiveness for investments in BiH is low due to low returns. Bureaucracy is creating additional operating costs and reducing opportunities for returns on investment.

---

<sup>13</sup> Goldstein, Ellen, Simon Davies, and Wolfgang Fengler. "Three reasons why the economy of Bosnia and Herzegovina is off balance." The Brookings Institution, November 5, 2015. <https://www.brookings.edu/blog/future-development/2015/11/05/three-reasons-why-the-economy-of-bosnia-and-herzegovina-is-off-balance/>

<sup>14</sup> Ibid.

FDI inflow amounted to 244 million euros in 2014, whereas the investments were mainly in three industry sectors: manufacturing, banking, and telecommunication (74 percent of all FDI stocks by industry from May 1994 until December 2015).<sup>15</sup> Generally, reforms designed to tackle the required reforms could increase the attractiveness of the local market for FDIs significantly. Net FDI inflows have covered just 31 percent of the cumulative current account deficit in 2008–2013, requiring the remaining financial debt to be met through new external indebtedness. Hence, gross external debt remained at around 50 percent of GDP, or 190 percent of export earnings and is forecasted to rise further in the near future.<sup>16</sup>

BiH has much to do not to be outpaced by its neighbors Croatia and Serbia. The fact that both of these economies are victims of the economic crisis supports BiH to not completely lose its connection to these two countries. Nevertheless, the fact that BiH has a smaller market and a much lower purchasing power compared to its neighbors, and an infrastructure that is far behind the requirements of a modern economy, it faces a backward position as soon as the economic crisis comes to an end.

Although Bosnia and Herzegovina is a developing a functioning market economy, and the government took actions to improve the business environment with regard to ease market entry and the granting of construction permits, the labor market remains largely unchanged. The unemployment rate is high, amounting to above 27 percent and rising to 63 percent among the youth population.

As BiH is at an early stage in achieving the capacity to cope with competitive pressure and foreign market forces, and in order to overhaul the business environment, it is imperative that the government reduces market rigidities, and especially that it reduces the tax wedge.

According to a World bank report, “on average, firms in Bosnia and Herzegovina make 45 tax payments a year, spend 420 hours a year filing, preparing and paying taxes and pay total taxes amounting to 23.3 percent of profit.”<sup>17</sup> Globally, Bosnia and Herzegovina stands 154<sup>th</sup> in a ranking of 189 economies on the ease of paying taxes.<sup>18</sup>

<sup>15</sup> Foreign Investment Promotion Agency of Bosnia and Herzegovina, <http://www.fipa.gov.ba/informacije/statistike/investicije/default.aspx?id=180&langTag=en-US>

<sup>16</sup> Country Report Bosnia and Herzegovina, *Euler Hermes Economic Research*, <http://www.eulerhermes.com/mediacenter/Lists/mediacenter-documents/Country-Report-Bosnia-Herzegovina.pdf>

<sup>17</sup> Worldbank, Doing Business 2016: Bosnia and Herzegovina, <http://documents.worldbank.org/curated/en/659921467991987957/pdf/100666-WP-Box393240B-PUBLIC-DB2016-BIH.pdf>

<sup>18</sup> *Ibid.*, p.71

It is not merely about the governance of public finances whose quality and sustainability have deteriorated during the past few years. There needs to be a complete reform of the tax system. BiH significantly reduced the taxes on profits in the past (today it belongs to the lowest in Europe—around 10 percent), simplified its labor tax processes, reduced employer contribution rates for social security, and abolished its payroll tax. Furthermore, it eased the administrative burden of filing and paying social security contributions by implementing electronic filing and payment systems.<sup>19</sup> Nevertheless, the tax on labor is one of the highest in Europe. Approximately, 65 percent of the income is taxed for social contributions and pension costs, thus resulting in a heavy shadow economy and tax avoidance. In my view, a strong decrease in taxing labor accompanied by an efficient monitoring system would lead to a boost in the budget and would increase spending. The high tax burden on labor has been identified as one of the biggest disruptive factors for doing business in BiH, and is not harmonized between the two entities and Brčko district. The taxation even has negative impacts on the mobility of labor force inside the country due to different regulations on health, pension, social and unemployment insurance. Not to mention that the tax administration reports are not used in a proper way to fight corruption (the topic “corruption” is a severe one in BiH seriously damaging the economy and prohibiting attractive investments; we will refrain from discussing it in this chapter).

Another big problem that the new reforms need to tackle, is the fact that the economy is more focused on consumption rather than on production.

During the post-war economic recovery, Bosnia and Herzegovina did not create new foundations for sustainable economic growth. Financial inflows and particularly aid and remittances—averaging around 20 percent of GDP—fueled consumption-based economic growth. Today, consumption remains at over 100 percent of GDP, with only a handful of countries having higher figures. To sustain high levels of income, create prosperity, and eliminate poverty, Bosnia and Herzegovina will need to shift toward an economic model built on production of goods and services rather than consumption.<sup>20</sup>

In order to overhaul the business environment, aside from reforms in the field of tax and labor governance, it is imperative that the rule of law is

---

<sup>19</sup> *Ibid.*, p. 72

<sup>20</sup> Goldstein, Ellen, Simon Davies, and Wolfgang Fengler. “Three reasons why the economy of Bosnia and Herzegovina is off balance.” *The Brookings Institution*, November 5, 2015.

significantly strengthened. The system of commercial law has to be improved and modernized. Property cases cannot wait for years to be resolved. According to a report of the European Commission, the average length of proceedings in 2014 was just over seven years for all courts across the country.<sup>21</sup> Comparing this data with Austria, where on average civil law suits take 4 months, and in Europe 9.5 months<sup>22</sup>, one can see that there is significant room for improvement in the Bosnian justice system. Furthermore, there has to be much greater consistency in court rulings. In the present circumstances, rulings are often completely different in cases that are remarkably similar.

Potential FDI is currently predominant in the energy and infrastructure sectors, as the energy sector is one of the strong sides of the local economy. BiH is the only country in the region that exports energy, and currently, many energy projects are still in the planning phase. For instance, RS recently signed a contract with the American company NGP for a feasibility study for hydro power plants with a total capacity of 365 MW aiming to invest up to 1.3 billion euros. Further energy projects foresee investments in the amount of around 4.2 billion euros. These investments include a thermal power plant project (value around 2.32 billion euros), a hydro power plant project (one billion euros), wind farm projects in the total amount of 831.5 million euros and small/mini hydro power plants projects totaling 63.5 million euros.<sup>23</sup>

A positive example of a realized project is the thermal power plant Stanari in RS. The EFT Group—a European company specialized in energy trading and investments, mainly active in Mid and Western Europe, Turkey and the Baltics—won an international tender for private partnership with the coal mine Stanari. Until July 2012, EFT invested 63 million euros in the modernization and enlargement of production of the coal mine. New equipment was bought including trucks, dumpers, bulldozers, diggers, fire department vessels and cars. More than 100 new jobs were created until now, all debts have been repaid, and the company doubled employee salaries. Local banks across the region were included to finance this investment.

---

<sup>21</sup> European Commission, Commission Staff Working Document, Bosnia and Herzegovina 2015, Brussels, November 10, 2015, p.15.

<sup>22</sup> Irma Ibrahimpašić, Master Thesis, “Die Effektivität des Gerichtswesens in Bosnien und Herzegowina im Vergleich mit Österreich”, pp. 90-91, <http://unipub.unigraz.at/obvugrhs/download/pdf/232248?originalFilename=true>

<sup>23</sup> Foreign Investment Promotion Agency of Bosnia and Herzegovina, <http://www.fipa.gov.ba/investinbih/index.htm>.

Infrastructure projects are the second biggest opportunity to enhance foreign and domestic investments. The FBiH published a tender for the construction of 350 kilometers of highway (the so called “Corridor 5c”), which should connect Budapest (Hungary)—Osijek (Croatia)—Sarajevo (BiH)—Ploče (Croatia). This highway would be the most important transit route in BiH, and the shortest line between Central Europe and the Adriatic Sea. More than 50 percent of the total population and roughly half of all economic activities of the country are situated along this highway route. As of yet, 100 kilometers of this road is already constructed. The government used the financing of international institutions, whereas construction companies mainly use funds through lending from local banks.

However, infrastructure projects do not only include new highways and roads to meet the challenges for a functioning corporate and SME environment. Aside from outdated infrastructure along border crossings, the water and electricity supply needs to be modernized or completely rebuild. To provide funds to these necessary measures, budget spending governance needs to be reviewed and put into a modern fiscal system, which will also guarantee transparency.

## **Conclusion**

Although banking in Bosnia and Herzegovina is a stable industry sector (despite its problems regarding high competition and regulatory affairs representing a burden for new capital injections), its continued attractiveness is highly dependent on the economic-political reforms aiming to improve domestic and FDI in future.

Key challenges for the government will be to increase public spending, attract new investments, and increase domestic demand. To do so, it is necessary to focus on improving its international country rating, leading to the reduction of high interest payments in the future. The basis for a prudent approach is an appropriate education system and a financially trained staff to structure future investments properly. Tax and labor law reforms are imminent. It is vital that improvements are not addressed only by new laws in place, but also by the appropriate bylaws that need to be passed in due time.

All in all, there are huge challenges ahead for local authorities in the near future. The application for EU candidature status is an important step in the right direction. Furthermore, the construction of the highway

is of utmost importance for the modernization of the infrastructure and one example of the pillars for further investments into this region. The government's reform agenda needs to be implemented on a daily basis, rather than a "marketing announcement" without any positive impact on the real economy. However, due to BiH's constitution and political reality, these processes cannot be carried out by institutions alone, but need strong support from outside.

## Chapter 6

# Overcoming Obstacles to Land Registration Reform in Bosnia and Herzegovina through Problem-Driven Iterative Adaptation

*Sean Parramore*

In 1995, Bosnia and Herzegovina's (BiH) land records were in disorder. The recent conflict<sup>1</sup> had distorted, destroyed or displaced records.<sup>2</sup> Records that could have proved ownership and which had survived, tended to be in a poor administrative state due to decades of neglect under socialism. Formally recorded exchange of land was therefore extremely difficult, yet there was no clear push for reform. This opacity around land records proved advantageous for some, who used informal reallocation of land to socially engineer postwar ethnic voting blocs.<sup>3</sup> These vested interests, not to mention the complicated politics and power structures established by the Dayton Peace Agreement, made it seem unlikely that land registration reform was forthcoming and that the opacity and dysfunction of land registration systems could be dealt with.

By 2015, the World Bank's Doing Business Index indicated that the ease of registering property had vastly improved between 2004 and 2015:<sup>4</sup>

---

<sup>1</sup> M. Garlick, "Protection for Property Rights: A partial solution?" *Refugee Survey Quarterly* (2000) UNHCR, pp.66-67

<sup>2</sup> According to Horisberger, World War II affected 20 percent of the mapping surveys held in the municipalities, which were not replaced after the war. J. Horisberger, "Land Administration in Bosnia and Herzegovina after the war," *Symposium on Land Administration in Post Conflict Areas*, Geneva (2004), p.4. In 2003, it was estimated that over a quarter had been destroyed in World War II and the 1992-95 wars. CRPC (Commission on Real Property Claims) (2004) End of Mandate Report (1996-2003), Sarajevo CRPC, Annex B, p.1.

<sup>3</sup> G. Tuathail, C. Dahlman, "*The West Bank of the Drina*": *Land Allocation and Ethnic Engineering in Republika Srpska*. Transactions, Institute of British Geographers (2006); A. Buyse, *Post-Conflict Housing Restitution: The European Human Rights Perspective with a Case Study on Bosnia and Herzegovina*, Ph.D. Leiden University (2008)

<sup>4</sup> In 2004, an average applicant interested in property registration needed seven procedures taking 331 days, and needed to pay 6.1 percent of the property's value. By 2015, he or she still needed to pass seven procedures, but now spent just 24 days at a cost of 5.2 percent of a property's value. Obradovic, Z. et al, "Towards sustainable land administration with improved customer service delivery," *World Bank Conference on Land and Poverty* (2016).

in 2016, the Bank ranked Bosnia and Herzegovina 97<sup>th</sup> (out of 189 countries)—one spot below Malta, and just twelve below France.<sup>5</sup> Bribery in the recording of real estate exchange was reportedly virtually non-existent, and satisfaction of land registration services was rising among public users.<sup>6</sup> By and large, outside evaluations showed that changes to rightful ownership were recorded systemically, expediently and accurately across the spectrum of the land registration system: on maps, local and central land ownership records. For those living in major cities in BiH, records on land rights were now accessible in a largely unified, digitized and increasingly harmonized system. Moreover, this system was now compatible across the Bosnian entities and with several of the EU's spatial data standards, even if this was not (yet) a formal accession requirement.<sup>7</sup> Land ownership was increasingly clear and formal real estate market activity was modestly increasing,<sup>8</sup> suggesting unrecorded land transfer was in decline.

This chapter analyses the process that led to a twenty year-long transformation of Bosnia and Herzegovina's land registration system. It uses mostly qualitative data to test two competing theories of institutional reform and explain how and why land registration reform in Bosnia and Herzegovina came about in the postwar period. It argues that the theory of problem-driven iterative adaptation (PDIA) best explains land registration reform in Bosnia and Herzegovina. It also posits that the importance of PDIA in this case illustrates both the possibilities and limits of economic reform in Bosnia and Herzegovina. This has implications for other reforms that are trying to open up and depoliticize control over the Bosnian economy.

---

<sup>5</sup> The Doing Business report of 2016 ranked Bosnia and Herzegovina 97<sup>th</sup> out of 189 economies in overall quality of property registration—<http://www.doingbusiness.org/data/exploreconomies/bosnia-and-herzegovina/>

<sup>6</sup> Three out of 143 surveyed users of land registry offices in the Federation noted “they had to make some informal payments,” while in the municipal cadastral departments this was five out of 151. The Federation of Bosnia And Herzegovina Federal Administration for Geodetic And Real Property Affairs, *The Eighth Quarterly Project Implementation Report For the period 01 July 2015 - 30 September 2015* (2015), p.38, p.53.

<sup>7</sup> Of all Western Balkans states, so far only Croatia was required to transpose the INSPIRE Directive pre-accession and to implement an INSPIRE roadmap post-accession. V. Cetl et. al. Report on the status of INSPIRE in the Balkan countries, *JRC Technical Reports*, European Commission (2013), p.8

<sup>8</sup> World Bank, Land Registration Project Final Report (2012), p.34, pp. 38-40.

## The Importance of Researching the Process of Land Registration Reform

Land registration is an activity directly related to cadastral mapping. It has become widely considered a bare necessity and cornerstone of any country formally committed to formal land markets.<sup>9</sup> There are many theoretical benefits of land registration reform:<sup>10</sup> land registration may provide clarity and authority on the question “who owns what?” Studies show<sup>11</sup> that if land owners feel protected against arbitrary expropriation; they may be incentivized to use land records to formally exchange their land (e.g., mortgaging, inheritance, etc.). Land registration may thus undermine informal exchange: corruption; land patronage; and a host of rent-seeking activities.<sup>12</sup> Voluntary, but relatively specific, standards have been developed by international organizations to set-up a land market-enabling registration system. A prominent example is the Doing Business Index,

---

<sup>9</sup> The “Cadastré” is “a parcel-based land information system that includes a geometric description of land parcels, usually represented on a cadastral map. In some jurisdictions, this is considered separate from, but linked to, the register of land rights and holders of those rights (land register), while in other jurisdictions the cadastre and land register are fully integrated.” Modern cadastres simply inform users of the physical extent of a property (the number, location and shape of each parcel and the “improvements” (i.e., buildings, roads etc.) as well information regarding ownership (consisting of 1) names register listing who holds what rights to these property units, and 2) legal archives—detailing the property unit’s location, origins and the interests behind it). It may also include the preceding history of transfer of a given parcel, including inheritance, decisions of verification and other changes of ownership. In a property rights regime that allows for market exchange, the textual part also covers taxable value besides ownership. J. Dorsey et. al., *An Assessment of Property Rights in Kosovo Final Report*, USAID, (2004), p.7. The ability of land surveyors (using orthography, aerial photogrammetry or satellite imaging) and land register clerks using computerized land registration systems to record, maintain, and update information about the physical dimensions and rights on land—as well as their ability to work together to make data uniform—is now considered crucial for any modern land registration system. See M. Higgins, *Positioning infrastructure and its relevance for sustainable land governance*. International Federation of surveyors (FIG) found in K. Deiniger et. al. *Innovations in land rights recognition, administration and governance* (2010), p.73.

<sup>10</sup> The case for land registration reform in developing and post-socialist countries was made most famously made in Hernando De Soto’s *Mystery of Capital* (2000). For some critiques and shortcomings of this theory, see E. Fernandes, *The Influence of de Soto’s The Mystery of Capital*, Lincoln Land Policy Institute (2002) and A. Gilbert, “On the Mystery of Capital and the Myths of H. de Soto: What Difference Does Legal Title Make?” *International Development Planning Review*, Volume 24, Issue 1.

<sup>11</sup> Ibid.

<sup>12</sup> L. Wren-Lewis “Corruption in Land Administration: Roles for Donors to Minimise the Problem,” *U4 Anti-Corruption Resource Center* (2013), pp.1-4.

which indicates a country's progress towards a measurable market-friendly order.<sup>13</sup>

Despite this seemingly crucial role in 2015 an estimated three in four people globally did not have access to formal land registration systems.<sup>14</sup> A cursory look at e.g. the Doing Business Index suggests that obstacles to establishing market-enabling land registration systems exist across the developed and developing world, including in post-socialist countries. Some of these problems are technical: an appropriate legal framework may not yet be in place, nor may common registration standards and procedures. In post-socialist countries, some laws may need to be removed, like legal bans or restrictions on private exchanges of land. Other technical problems may be that real estate records were not updated for a long time; or they may be incomplete. Clerks and surveyors may be poorly trained and prepared to use modern recording software and surveying technology.<sup>15</sup> However, the core literature on land governance already suggests that it would be a mistake to perceive dysfunctional land registration as a purely technical or capability problem.<sup>16</sup> Laws can be rewritten; donors can provide funds to build capacity. The key seems to be to win over local governing elites to adopt and enable land registration reform<sup>17</sup>.

Engendering political acceptance to reform land registration for the sake of markets seems to be a particular challenge in post-socialist and post-conflict countries. In post-socialist Central Eastern Europe “land [...] markets have evolved where governments have allowed them” noted the economist Anders Aslund, and where they did, they emerged over a long period of time.<sup>18</sup> Country studies confirmed this notion.<sup>19</sup> In post-conflict countries, the resistance to market-enabling land registration

---

<sup>13</sup> In addition, most developing countries' overall progress is now explicitly measured in the World Bank's Doing Business Index and implicitly in the Sustainable Development Goals. See footnote 5; <https://sustainabledevelopment.un.org/sdg15> and <https://sustainabledevelopment.un.org/sdg11>

<sup>14</sup> Mennen, Tiernan. “Know Your SDGs: Land Matters for Sustainable Development.” September 2, 2015. <http://blog.chemonics.com/know-your-sdgs:-land-matters-for-sustainable-development>.

<sup>15</sup> K. Deiniger et al. *Innovations in land rights recognition, administration and governance*. 2010.

<sup>16</sup> Hernando De Soto. *Mystery of Capital: why capitalism triumphs and fails everywhere else*. 2000.

<sup>17</sup> Hernando De Soto. *Mystery of Capital: why capitalism triumphs and fails everywhere else*. 2000.

<sup>18</sup> A. Aslund, *How Capitalism Was Built: The Transformation of Central and Eastern Europe, Russia, the Caucasus, and Central Asia*. (2012), pp.186-187

<sup>19</sup> E.g. see F. Harvey, *Elasticity Between the Cadastre and Land Tenure: Balancing Civil and Political Society Interests in Poland* (2006)

reform may be even more formidable compared to post-socialist countries. Rival groups during or after conflict may have engaged in the destruction or distortion of proof of rights on real estate and set themselves up for informal positions of power. Once in such a position, they might be tempted to delay processes to return the pre-war distribution of these rights.<sup>20</sup> Worse yet, donors may be too concerned with maintaining political stability to insist on market-enabling, ownership clarifying land registration reform.<sup>21</sup>

Many have noted how the incomplete transitions from conflict and Yugoslav socialism left enduring institutional problems and vested interests in keeping many parts of the economy unreformed. This incentivized “state capture” by a few politically networked businesses and political individuals who ensure state institutions benefit no one but insiders.<sup>22</sup> As these networks appeared wedded to the political, economic, and institutional *status quo*, BiH seemed to resemble a “limited access order.”<sup>23</sup> In such a context it seemed reasonable to expect little space for reforms, including in land registration, to push the country towards a more “open access order.”<sup>24</sup> Since 2006, domestic and external decision-makers have made attempts at institutional reforms pertinent to European integration and other (economic) reform agendas. The tendency of these attempts to fail led many observers to take a bleak view about the possibilities of institutional reform in Bosnia and Herzegovina.<sup>25</sup>

<sup>20</sup> S. Leckie and C. Huggins, *Conflict and Housing, Land and Property Rights: A Handbook on Issues, Frameworks and Solutions* (Cambridge University Press, 2011), pp.185-186. For example, in Kosovo most land records and map were taken to Serbia after the conflict. Similar destruction or removal happened in the wake of conflicts in Timor Leste and Cambodia. D. Todorovski et al., *Post-conflict land administration; a facilitator of the post-conflict state building the case of Timor-Leste*. FIG conference paper (2015).

<sup>21</sup> D. Zaum and C. Cheng, ‘Corruption and post-conflict peacebuilding: Selling the peace?’ Routledge (2011), p.14-15; R. Biddulph. ‘Cambodia’s Land Management and Administration Project’ (2014)

<sup>22</sup> S. Blagovcanin and B. Divjak 2015, *How Bosnia’s Political Economy Holds It Back And What to Do About It*, Johns Hopkins University SAIS Centre for Transatlantic Relations, p.14.

<sup>23</sup> A post-conflict limited access orders is a society where governing elites deliberately keep access to basic public services to the economy limited to a select group of political insiders. D. North, ‘A conceptual framework for interpreting recorded human history’, No. w12795). National Bureau of Economic Research (2006).

<sup>24</sup> D. North et. al., *Limited Access Orders: Rethinking the Problems of Development and Violence* (2011).

<sup>25</sup> S. Toperich and M. Kaménica, ‘Challenges of Democracy in Bosnia and Herzegovina’ in A. Noi and S. Toperich, ‘Challenges of Democracy in the European Union and its Neighbors’, Center for Transatlantic Relations– Johns Hopkins University SAIS (2016); F. Bieber,

## Theories of Institutional Reform

How then to explain the transformation of land registration system in Bosnia and Herzegovina? If the general assessment is that Bosnia and Herzegovina is a limited access order, why and how would general obstacles to institutional reform be overcome?

Matt Andrews and a team of researchers at the Harvard Kennedy School of Government suggest two competing theories of institutional reform that help explain the chapter's questions of why and how institutional reform may happen in post-conflict countries. Especially given that in post-conflict countries such reforms seem unlikely to be adopted, and let alone be implemented.<sup>26</sup> Both theories expect the reform method to break an entrenched *status quo*—or “capability trap”<sup>27</sup>—in which governing elites are unable or unwilling to break out of a vicious circle of “corruption” and state dysfunction (like the limited access order mentioned above).

The first theory and reform method is the solution-based and leader-driven change (SLDC) theory. Here one expects institutional reform to achieve the intended results because:

solutions are fully identified up-front and are the focus of change; the reform is fully planned out at the start and implemented as planned; a champion drives the process; and a pure-form best practice solution is produced.<sup>28</sup>

The second theory of institutional reform is called problem-driven iterative adaptation (PDIA). It:

proposes that successful change is usually motivated by a problem, not a solution; the reform content emerges through a process of experimentation and trial and error; with multiple agents playing

---

‘Building Impossible States? State-Building Strategies and EU Membership in the Western Balkans’, *Europe-Asia Studies* (2011); G. Noutcheva, ‘Fake, partial and imposed compliance: the limits of the EU’s normative power in the Western Balkans’, *Journal of European Public Policy* (2009).

<sup>26</sup> M. Andrews, ‘Explaining Positive Deviance in Public Sector Reforms in Development’, *World Development*, Vol. 74 (2015); M. Andrews et al. ‘Development as Leadership-led Change’, Kennedy School of Government Harvard University (2010);

<sup>27</sup> M. Andrews et al., ‘Escaping Capability Traps through Problem-Driven Iterative Adaptation’ Harvard Kennedy School Faculty Research Working Paper Series (2012)

<sup>28</sup> Andrews (2015), p.199

different leadership roles [within a reform coalition]; producing a mixed-form hybrid that is fitted to the peculiar context.<sup>29</sup>

Thus in the case of SLDC the drivers of such a change are preconceived regardless of the context: this can be a technological standard or best practice imported from outside (like the World Bank's Doing Business Index on property registration or perhaps supported by a concessional loan or other forms of donor support). Or, there may be external incentives to change, such as (new) EU accession requirements.<sup>30</sup> The PDIA reform emerges from problems—a disruption—like an economic crisis. In this situation, a solution is not predetermined but emerges through (domestic and external) actors cooperating in order to adapt the institutional context incrementally.<sup>31</sup>

The two theories have competing hypotheses to the questions of why and how institutional reform may happen. Below the questions and hypotheses of research are diagrammatically depicted and adapted to the case at hand.

## Methodology

To test these theories, the chapter relies on data acquired between October and December 2015, through semi-structured interviews and primary sources. The data is organized and analyzed using the process tracing method.<sup>32</sup>

---

<sup>29</sup> Ibid, p.200

<sup>30</sup> F. Schimmelfennig, and U. Sedelmeier, Governance by Conditionality: EU Rule Transfer to the Candidate Countries of Central and Eastern Europe. *Journal of European Public Policy*, Vol. 11, Issue 4 (2004).

<sup>31</sup> Andrews (2015), p.204; Andrews et. al. (2010), p.9.

<sup>32</sup> Process tracing allows one to observe a particular case's historical context and to identify steps that led to a certain outcome—here principally the improvement of DBI scores). A. George, & A. Bennett, *Process-tracing and historical explanation*, Case studies and theory development in the social sciences (2005). The method allows for finding out original historical causes and processes that drove unlikely outcomes, and description of how intervening variables interacted and in what sequence they had impact P. Vennesson, *Process Tracing and Historical Inquiry: Policy-Making Sequences and 'Possibilism'* European University Institute (2010). Quantitative data suggesting correlation can be used alongside qualitative data to interpret how and why the outcome manifests itself. Finally, this method has been considered appropriate in countries like Bosnia and Herzegovina where outside actors are structurally positioned to influence domestic actors, reform processes and institutional outcomes

**Table 1. Hypotheses of SLDC and PDIA (H1-8)—adapted from Andrews (2015)**

<b>Key question</b>	<b>Solution and leader-driven</b>	<b>Problem-driven iterative</b>
1. What drives post-war land registration reform?	H1. Land registration reform is driven by a solution. Data shows the solution is identified and derived from a known (external) technical standard, best practice and/or a legal standard.	H5. Land registration reform is driven by an identified problem. Data shows disruptions like an economic or political crisis to kick-start a search for possible solutions.
2a. Who leads the post-war land registration reform process?	H2. Land registration reform “is led by a high-level individual or institution with authority.” One expects data to underline the central and indispensable importance this leader throughout the reform process.	H6. Land registration reform is led by a group of actors who play different “functional roles” in the reform process. One expects data to recognize playing these roles in the adoption and/or implementation process.
2b. How do post-war land registration reforms get implemented?	H3. Land registration reform is implemented according to a plan of action specified in advance. Data shows implementation occurs in accordance with this plan.	H7. Land registration reform is implemented through trial and error. Data suggest local actors finding suitable reform content and adapt it to the local reality.
3. What do post-war land registration governance outcomes resemble?	H4. The outcome of land registration reform resembles the preconceived solutions. Performance indicators like the Doing Business Index suggest implemented solutions meet standards. The case suggests an open access order (OAO) can be approximated regardless of local political preferences.	H8. Land registration reforms resemble products of adaptation. Data reveals implemented solutions as blends of local and external ideas. The case suggests incremental advance towards best practice or even an OAO is politically acceptable if domestic ideas and political interests are accounted for.

## Origins of the Problem of Unclear Land Records

The postwar problem of unclear land records in Bosnia and Herzegovina arguably starts in the Austro-Hungarian period. When the Austro-Hungarians came to govern Bosnia and Herzegovina in the late 19<sup>th</sup> century, they did not expropriate or redistribute land; instead they decided to record ownership of existing rights on land more efficiently, systematically and accountably than the Ottomans had.<sup>33</sup> The system for doing so became commonly known as the “Grunt”. It consisted of two separate books: one book recording the rights on property within a numbered parcel—also called the land book or land registry. This book was kept in courts. The other book was the land survey, showing the same parcel graphically depicting its shape, size and structures kept by cadastral officials. This system survived the 20<sup>th</sup> century’s political transformations up to and beyond the post-1995 era. Marshal Tito, Yugoslavia’s long-time head of state, had not abolished the Grunt nor had he completely outlawed private land ownership (see below). In principal, the Grunt therefore remained the central authority on questions about “who owns what.” In practice, the Grunt was unable to keep track of changes of the reality of land ownership. One of the chief causes was redistributive justice and land re-allocation: under the Yugoslav Kingdom, land was redistributed from large to small landholders; whereas under the early Socialist Federal Republic of Bosnia and Herzegovina from private owners to nationalized socially-owned enterprises. In addition, at the end of the Yugoslav period there were partial privatizations of socially owned real estate (e.g., military apartments).<sup>34</sup> These re-allocations were not systematically recorded in the Grunt’s land books.<sup>35</sup>

Besides, the political transitions and land redistributions increasing legal fragmentation made the reality of land ownership different from the official records. One reason for this fragmentation was that Tito introduced limited private land ownership to a maximum of ten hectares or less. Credit restrictions and associated tax obligations gave private land owners little economic incentive to register their ownership.<sup>36</sup> Legal fragmentation

<sup>33</sup> Wikileaks Bosnia: Consular Fraud Perspectives On Niv Applicants. Land Ownership Documents, *wikileaks cable* (2009), [https://wikileaks.org/plusd/cables/09SARAJEVO1404\\_a.html](https://wikileaks.org/plusd/cables/09SARAJEVO1404_a.html)

<sup>34</sup> CRPC (2004).

<sup>35</sup> Wikileaks (2009).

<sup>36</sup> Smallholder farming became so common that it was the only sector which was predominantly privately owned. By 1983, eighty-three percent of agricultural land in the SFRY was owned by approximately two-and-a-half million individual farmers. World Bank, *Staff Ap-*

was made worse as Tito also introduced a separate system, known as the “Katastar.” This was in order to register possession and user rights on socialized land, buildings and apartments. The Katastar’s records were linked to aerial surveys which tended to be graphically more accurate compared to the old surveys of the Grunt.<sup>37</sup> Thus an effort was made to harmonize the Grunt survey and records with the Katastar’s surveys and records. This was made to bring BiH’s land registration systems within a single centralized system, the Real Estate Cadastre (REC). However, when just ten percent of the municipalities had completed the process of creating the REC,<sup>38</sup> the war that started in 1992 halted any further progress.

The war worsened the already inaccurate land registration systems. “[C]ontrol of territory was a major [...] rationale for which the war was fought”<sup>39</sup>; and belligerents took advantage of controlling records on pre-war distribution of ownership and possession rights. Many of the Grunt’s land books were destroyed—others were “altered” or spirited away across entity or international boundaries. Just one-third of ownership records held in courts were still “intact” at the war’s end. The Katastar’s possession lists were also manipulated: “With a gun in one’s face” many possessors were forced to legally transfer their property. As roughly one in four Bosnians were displaced, many found shelter in abandoned homes, and “[m]any property transfers made during and immediately after the war were disputed.”<sup>40</sup> At the same time, land and housing became increasingly scarce.<sup>41</sup>

## Restitution and the Postwar Path Towards Recognition

The signatories of the November 1995 Dayton Peace Agreement—which included the two warring entities—Republika Srpska (RS) and the Federation of Bosnia and Herzegovina (FBiH)—were faced with many problems of political prioritization. Re-launching the attempt at an REC or finding an alternative way to create a systematic recording of land records was not among their priorities.<sup>42</sup> However, real estate did enter

---

*praisal Report Kosovo Regional Development Project* (1983), pp.1-2. World Bank Land Registration Project Appraisal (2006), pp.1-2.

<sup>37</sup> Wikileaks (2009)

<sup>38</sup> CRPC, Annex D (2004), p.1. Horisberger (2004), estimates around 10 percent, p.7.

<sup>39</sup> Garlick (2000), pp.66-67

<sup>40</sup> CRPC (2004), Annex B and D.

<sup>41</sup> Garlick (2000), pp.66-67

<sup>42</sup> There is no known evidence that a plan existed to clarify and formally divide the responsibilities for gathering land records, verifying it and making it accessible in each entity.

the Dayton accord in some way, as the signatories committed to clarify the rights associated with the problem of displacement. A special independent<sup>43</sup> body, the Commission for Real Property Claims of Displaced Persons (CRPC), was mandated to “receive and decide any claims for real property [...] not voluntarily [...] transferred since April 1, 1992.”<sup>44</sup> The entities were required to cooperate and give the CRPC access to land records; to make any legal adjustments and provide financial, technical and human resource support to enable the CRPC’s work.<sup>45</sup>

However, soon after the first CRPC members settled in Sarajevo in March 1996, they learned about the technical and political difficulties they would face. Their primary working material—the information contained in the three different land registration systems—was at odds with the reality of ownership on the ground. They learned this was the result of the waves of redistributive justice, destruction, and neglect, that had caused havoc for the land records: it was not uncommon that the last registered “current” owner of a plot of land was an Austro-Hungarian citizen. They also learned about the discordant land registration systems themselves: one for ownership rights—the Grunt imported from Vienna—another, the Katastar for possession rights—a legacy from Socialist Yugoslavia—and the REC. Finding evidence to decide a restitution case in this institutional landscape would prove difficult enough. Yet even if the CRPC staff knew where to secure pre-war data on possession of property, they ultimately depended on political cooperation and approval of individual municipalities to disclose this data. This cooperation functioned in some municipalities,<sup>46</sup> yet in others, like Banja Luka, “a pattern of obstruction” was discernable.<sup>47</sup> Political obstruction also existed at the legislative level. Despite their Dayton-imposed obligation to cooperate, lawmakers

<sup>43</sup> The CRPC had a 9-member decision-making body. Two members were appointed by RS, 4 by the Federation and 3 by the President of the European Court of Human Rights and designated one as Chairman. Dayton Peace Agreement, Annex 7, Article IX (1995).

<sup>44</sup> Dayton added that “where the claimant does not now enjoy possession of that property [...] for return [...] or for just compensation.” Dayton Peace Agreement, Annex 7, Article XI (1995).

<sup>45</sup> C. Rabenhorst, *The Real Estate Market in Bosnia and Herzegovina. Current status and recommendations for reform*, the Urban Institute (2000).

<sup>46</sup> CRPC (2004), Annex D, pp.5-6.

<sup>47</sup> Especially when it came to data that could enable repossession of socially-owned apartments, the capital of RS shared very little useable evidence with the CRPC. Its municipal “representatives” simply stated that “relevant documentation” was destroyed. The CRPC confided retroactively that the Geodetic Authority of the RS (the institution that oversees and verifies all cadastral data collection within RS-borders (also based in Banja Luka) had resisted “from the beginning of the CRPC’s work.”

in both entities had enacted and sought to uphold legislation that essentially prevented refugee returns and perpetuated political control over abandoned real estate.<sup>48</sup> Even where the CRPC managed to reach a decision on restituting property, it was obstructed from implementing it.<sup>49</sup>

The Peace Implementation Council (PIC) (the body representing the G7, the EU Presidency, Russia and Turkey, which through a Steering Board appointed a High Representative) realized the lack of restitution was stranding hundreds of thousands of displaced in third countries.<sup>50</sup> After four years of ensuring the implementation of the Dayton Agreement, the PIC realized this key Dayton priority was not met. In May 2000, the PIC openly recognized that commonplace domestic political obstruction of enabling restitution was reflective of a larger problem: the unwillingness of domestic politicians to relinquish control over unclaimed or unrecorded yet valuable economic resources, notably scarce housing and land. The lack of clarity on ownership rights was also being recognized as economically unsustainable: the prospect of Bosnia and Herzegovina remaining a “donor dependent economy” loomed in anticipation of donors’ impending decampment and withdrawal of donors funds on which postwar economy recovery had significantly depended.<sup>51</sup> Now that the failure to enable returns and restitution was becoming evident, the economic problem of opacity around land ownership rights was linked to the paltry levels of foreign direct investment (FDI). With land records still in a state of disrepair and confusion, foreign investors who could not be sure the real estate on which they wished to invest was legally secure. The PIC thus demanded

<sup>48</sup> From the moment it started in March 1996 work the CRPC was understaffed (10 officials) and in search of alternative funding from donors. Until the end of its mandate in 2003, the CRPC was dependent on donor funding, and hard-pressed to secure it. The entities provided no financial support. CRPC (2004).

<sup>49</sup> A report delivered to the OHR by USAID-paid consultants in January 2000 noted: “CRPC decisions [...] do not necessarily result in eviction of unlawful occupants, in updating the land register or in enabling the decision holder to sell or otherwise dispose of the property. Often, they are frustrated by local judges, politicians or other officials whose co-operation is needed ... [this] is exacerbated by lack of alternative accommodations for evictees as well as by political considerations. Rabenhorst (2000), p. 5.

<sup>50</sup> A CRPC report noted that “[f]our years after the GFAP [Dayton] was signed, it is estimated that up to 830,800 people (487,300 in the FBiH and 343,500 in Republika Srpska) remain displaced within Bosnia and Herzegovina 324,100 refugees remain in host countries without durable solutions. Many, if not most, wish to return to the property that they occupied prior to the war (CRPC 1999, p.1).

<sup>51</sup> A “self-sustainable market-orientated economy cannot be built in an environment where the principles of economic logic are overruled by the objectives of maintaining political control.” <http://ec.europa.eu/enlargement/archives/seerecon/calendar/2000/events/c20000523.htm>

BiH's governing elites to enact a land registration reform to deal with this problem.<sup>52</sup>

The effort to encourage domestic lawmakers to start this reform lasted two years—up to 2002. A bevy of donors, principally GIZ (the German Development Agency) helped fund the search for a solution, and together with lawyers and geodetic experts they met in stakeholder consultation meetings. Yet after two years they still could not agree over whether land registration powers should be separated (i.e., with land registries and survey separated as under the Grunt) or centralized under one institution (as under the REC). Separation would ensure more accountability; while centralization more administrative efficiency. Lawyers tended to favor the separated system. Conversely, cadastral experts tended to favor the administrative efficiency and expediency of having “an integrated solution under the roof of the geodetic administrations.” GIZ was involved in these deliberations on drafting a new law, yet it did impose any particular draft or standard.<sup>53</sup> No other donors had a standard or best practice to hold up to the lawmakers (the World Bank had yet to establish its Doing Business Index and the EU lacked an *acquis* in this area.)<sup>54</sup>

Without an agreement on a new land registry law in either entity, a new High Representative, Paddy Ashdown, soon after assuming office in May 2002, urged action “to remove barriers to business [...] by restoring confidence in ownership and investment.”<sup>55</sup> The PIC steering board now

---

<sup>52</sup> Ibid.

<sup>53</sup> GIZ, *Land Management and Land Administration Projects in Southeastern Europe Good practices and lessons learned from two decades of GIZ Engagement* (2015), p.23.

<sup>54</sup> Since its inception, the EU principle has been that “[t]he Treaties shall in no way prejudice the rules in Member States governing the system of property ownership”. <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A61998CC0367>. As long as Member States do not discriminate, they are entitled to design their own systems of how land is owned, used and acquired. European Court of Justice Case 182/83, *Robert Fearon and Company Ltd v. The Irish Land Commission*, judgment of 6 November 1984, (1984). Found in A. Mungiu-Pippidi and L. Stefan, *Perpetual Transitions Contentious Property and Europeanization in South-Eastern Europe East European Politics and Societies Volume 26* (2012), p.356. From 2007, the INSPIRE directive set some guidelines for spatial data infrastructure, but for Bosnia and Herzegovina these were optional. Cetl (2013).

<sup>55</sup> Ashdown set out to form a “Justice and Jobs” agenda the month he arrived. It consisted of 10 pledges and 67 commitments one of which aimed “to remove barriers to business [...] by restoring confidence in ownership and investment.” The document read that it had been prepared together with the Council of Ministers (A body of state-level ministers’ whose prime minister is nominated by the elected three-headed Presidency of Bosnia and Herzegovina) Office of the High Representative (OHR), ‘Jobs and Justice: Our Agenda’ (2002), p.2. Elsewhere it is argued that the OHR wrote the programme unilaterally—see e.g. G. Knaus and F. Martin, ‘Travails of the European Raj’ (2003).

made it “legally binding” for “future governments” of RS and the FBiH<sup>56</sup> to “enact harmonized land registry laws” and to subsequently “secure technical assistance in training and staffing land registry offices.”<sup>57</sup> Still, the call for land registration reform was ignored: it was an election year. After the general elections in October, Ashdown saw no sign the reforms would soon be adopted by the domestic legislatures of the RS and FBiH entities. In a letter dated Friday October 18, 2002, addressed to the UN Secretary General, Ashdown speculated that the government formation process would be “perhaps lengthy” and expressed alarm at the economic cost of slow reform:

Donor contributions are falling, foreign and domestic debt is increasing, and there is little or no foreign investment to fill the gap. By next Spring, BiH could be in the grip of a severe domestic debt crisis. The country is racing against time, and *there is no choice* but to increase the pace of economic reform. [...] BiH still needs [...] a Law on Land Registry Books.

The next Monday, Ashdown wrote to the members of the RS and FBiH parliaments: He reminded them that the PIC had required twice in the past two years to pass this law. He explained, a final time, that it was “a necessary precondition [...] for economic development and investment.” Moreover, “any further delay” in adopting the law would “threaten [...] natural persons” property rights. After the entity lawmakers failed to react, Ashdown used his PIC-granted powers to singlehandedly impose the Law on Land Registry in both entities.<sup>58</sup>

## Towards Implementation

Ashdown’s imposition of the land registry law was game-changing for three reasons. First, the law separated responsibilities for handling survey

---

<sup>56</sup> Bosnia: Report by the High Representative for the Implementation of the Peace Agreement to the Secretary-General (S/2002/1176)

<sup>57</sup> OHR, (2002), p.7, p.12.

<sup>58</sup> In the decision, Ashdown cited the entities requirement to adopt the law as stated in the PIC’s May 2000 conclusions and the Steering Board’s July 2002 decision. OHR, *Decision Enacting the Law On Land Registry Federation Of Bosnia And Herzegovina*, Number 58/02 (2002) [http://www.fbihvlada.gov.ba/bosanski/zakoni/2002/odluke%20VP/56\\_bos.htm](http://www.fbihvlada.gov.ba/bosanski/zakoni/2002/odluke%20VP/56_bos.htm). The same law - The Law on Land Registry of the Republika Srpska - was imposed in the RS, no. 67/03. Gotovusa et. al, *Zakoni o katastru Republike Srpske: politic\_ko poigravanje pravom na imovinu* (2012)

and land record data. This clarified the institutional framework of land registration while also making horizontal cooperation between a range of actors a prerequisite for its implementation. Ashdown's law clarified responsibilities by essentially reinstating the Grunt's two-book system. The maintenance of the land (registry) books would solely be the responsibility of land registry offices in forty-eight first instance courts across Bosnia and Herzegovina, each overseen by a court president.<sup>59</sup>

This, on the other hand, complicated the task of clarifying the land records by updating and harmonizing the data and the different systems that existed across the country. The cadastral (or geodetic) administrations that oversaw the land surveys and spatial information were headed by a director, and supervised and funded by the ministry of justice of each entity. The land registry offices were in a different hierarchy.<sup>60</sup> Court presidents directed the land registry offices and a state-level body oversaw their work.<sup>61</sup> The law thus ensured that the task of devising plans for implementation depended on several parallel hierarchies within—and across entities.<sup>62</sup> It required justice ministers and geodetic administration on the one hand, and court presidents and land registry offices on the other, to cooperate horizontally and to prioritize the search for solutions

---

<sup>59</sup> The laws on land registry were the foundation for kick starting the land registries reform process. Other relevant laws are the law on cadastre and the law on real rights. See S. Leskovic et. al. *Registering Property—Experience from Bosnia and Herzegovina*; <http://www.klix.ba/vijesti/bih/registracija-zemljista-u-fbih-za-uredjenje-imovinskopravnih-odnosa/100916077>

<sup>60</sup> At the top of the hierarchies were the geodetic authorities of each entity, headed by a director who was appointed by, and received funds from, the entity's minister of justice.

<sup>61</sup> The court presidents in turn were appointed by the High Judicial and Prosecutorial Council (HJPC)—a state-level institution—which carried out this work. The HJPC was also legislatively imposed by Ashdown's predecessor, High Representative Petritsch shortly before the former's arrival. Ashdown letter to UNSG (2002), p.6. The HJPC law entered into force June 2004. <http://pravosudje.ba/vstv/faces/vijesti.jsp?id=51991>

<sup>62</sup> In RS and Brčko, the cadastral administration was more centralized by virtue of those regions' political structure. In RS, the Ministry of Justice supervised and funded the entities' Geodetic Administration, which in turn did the same for the different cadastral municipalities (each cadastral municipality covering a number of political municipalities). In Brčko the head of the department of public register partly fulfilled this function. Interview, Belmir Agić, formerly in charge of Public Register dpt. on behalf of the Brčko government, Sarajevo. In the FBiH, the cantonal ministries of justice and geodetic administrations were funded by the canton. Thus, while RS and Brčko could work hierarchically, the Federation Geodetic Administration (FGU) had to coordinate horizontally, i.e., network to enforce compliance with the quality standards. Interview, Tomislav Tomić, Expert Advisor for Cadastral Affairs, Federal Administration for Geodetic and Real Property Affairs, FGU Sarajevo.

to clarify land records.<sup>63</sup> This willingness existed and the subsequent horizontal cooperation was strong. Court presidents and geodetic administrations invested in building and maintaining positive working relationships, and incrementally worked towards fully updated and integrated systems.<sup>64</sup> Certain court presidents turned out to be particularly strong allies for this effort.<sup>65</sup> Similarly, the entity ministers were politically committed to work towards a fully updated and unified system. Their “leadership, “oversight” and “engagement” were seen to have a strong “motivational effect” to realize the project goals on lower administrative levels. Cooperation between the entity ministers was considered strong.<sup>66</sup>

The second game-changing effect of Ashdown’s law was that it attracted a stream of international donor support for the process of clarifying land records. Shortly after the law was adopted, the so-called Land Administration Project (LAP) was created with financing from Germany (GIZ), Sweden (SIDA), and Austria for the ministries of justice and geodetic administrations of FBiH and RS. LAP began to re-educate land registry and cadastral officials “with the aim of improving efficiency and quality of the provision of services to users.”<sup>67</sup> In 2006, the entities agreed to a 15 million USD concessional loan from the World Bank Land Registration

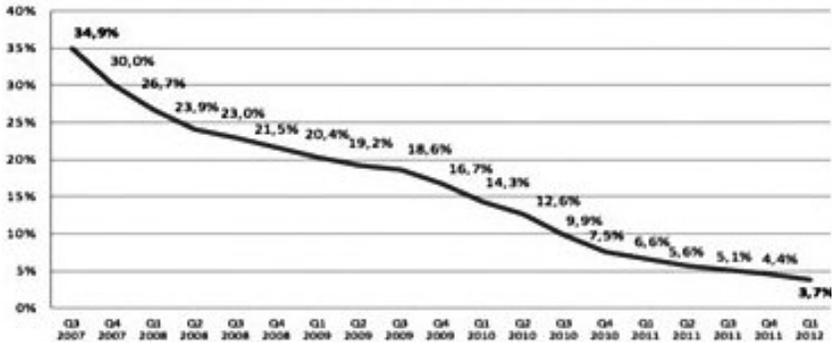
<sup>63</sup> Interview, Sarajevo. October 14, 2015; November 30, 2015.

<sup>64</sup> Interview, Sarajevo. October 14, 2015; November 30, 2015.

<sup>65</sup> Such as the President of the Sarajevo Court, Goran Salihović, President of the Municipal Court in Sarajevo (September 1, 2005 - 2013). The latter secured resources from the Ministry of Justice to pay for his court’s land registry office refurbishment. He also made a lighter version of land administration system (LARIS) (i.e., not all data) version freely accessible to the public. He also advised on the Federation BiH Ministry of Justice on the implementation of donor-funded projects (See below). <http://www.tuzilastvobih.gov.ba/?id=66&jezik=e&kat=15&opcija=sadrzaj>. Interview, Sarajevo. November 30, 2015.

<sup>66</sup> The Ministries of Justice of the Federation, Feliks Vidovic from 2007 and 2011 was heavily engaged in attaining progress in the LRP. <http://imovinapoliticara.cin.ba/biography.php?id=92>. Interview, Sarajevo. October 14, 2015; November 30, 2015. See also: <http://www.ustavnisud.org/Sudija.aspx?sudija=13&cat=11&subcat=42&id=37&lang=bos>

<sup>67</sup> GIZ was not coincidentally the primary donor of implementation as it built on the experience of its capacity building pilot projects in 1999 to 2001, and its involvement in the two stakeholder consultations of the new land registry draft law. Now with more resources available it could field a much larger, multidisciplinary team of legal, cadastral, IT and PR experts. Sida co-financed since 2003; ADA since 2004. World Bank, Appraisal Document LRP (2006), p.19 The total amount funded by LAP was 8.8 for the Federation and 6.2 for RS. The entities themselves provided 1,225 and 0 reportededly valuateplementation of ders involved.onentities, orities:viate local housing shortages. standards or consistent s,9 million USD respectively. Additional donors paid 5,4 million euros 2010 (2010 Bosnia And Herzegovina Federation Of Bosnia And Herzegovina Federal Ministry Of Justice Of Sarajevo, Project Implementation Unit of the World Bank for Land Registry Administration in the Federal Ministry of Justice; GIZ (2015), pp.25-26

**Figure 1. Pending requests at land registration offices drop from 2007**

Source: The World Bank (2012).<sup>68</sup>

Project (LRP) to improve technical infrastructure for the registration and clarification of land records in cooperation with the LAP.<sup>68</sup> Both projects avoided imposing severely restrictive measures. Instead they took a “pragmatic, incremental, approach applied to software development and [...] use[d] [...] small contracts to deliver specific outputs”—i.e. new monitoring and evaluation systems, new land recording and geospatial information systems were not installed all at once.<sup>69</sup> Transaction costs began to fall as the number of pending requests dropped and incentives to informally expedite the registration process (bribery) were further reduced through digitization<sup>70</sup> (see graph 1 below). This reduction meant that citizens, banks and notaries could spend less time and money to acquire excerpts related to specific property—e.g. for a mortgage.<sup>71</sup> The LRP and LAP

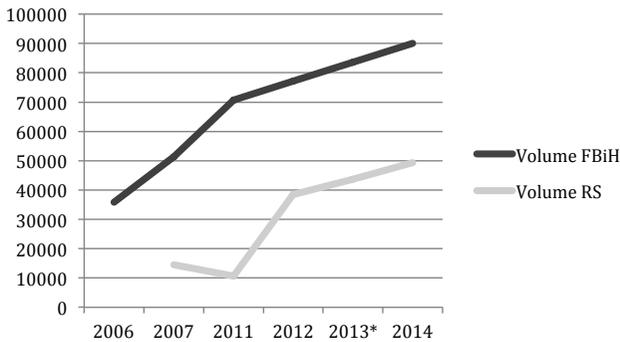
<sup>68</sup> World Bank (2012)

<sup>69</sup> The World Bank claimed these successes could be explained in part by “good court presidents, managers and staff” responding “positively” to the revolution in their workplace (“renovations, new equipment, improved software, temporary additional staff and training” provided by the LRP and LAP). *World Bank LRP final report* (2012), p.6.

<sup>70</sup> A new digital archive system—LARIS—forced land clerks to process cases chronologically, which according to GIZ and the FGU added “more transparency to the process” and reduced the incentive for bribery. “The development and nationwide implementation of new software for the land registry “LARIS” essentially improved the land registry data management and data exchanges with other institutions (like banks and notaries): “the accompanying increase in transparency was an important step against corruption.” *GIZ* (2015). p.23.

<sup>71</sup> GIZ (2010); Interview, Sarajevo. October 14, 2015; November 30, 2015.

**Figure 2. Registered transactions spike in 2011–12 (volume in thousands)**



Source: The World Bank (2012, 2016); RS Geodetic authority (2015); author's calculations for year 2013.

support for instrumentalism was key to this gradual improvement according to both the RS and Federation authorities.<sup>72</sup>

GIZ invested in encouraging citizens to use land registration services,<sup>73</sup> and as backlogs continued to drop satisfaction rose among primary users of land registration services (banks, notaries) and the number of formal real estate transactions began to increase.<sup>74</sup> As backlogs dropped and property registration time fell to twenty-five days, registered transactions spiked in 2011–2012<sup>75</sup> (see Figure 2).<sup>76</sup>

<sup>72</sup> Idem.

<sup>73</sup> It began to focus on public outreach to encourage use of the reformed registries to overcome predominant views that its services were expensive and time-consuming, while encouraging citizens to use the LARIS system (it was found that particularly made good use of it and merged with cadastral project). G. Schnindler, *Project experiences with land management in countries in transition*. (2006), pp.12-13; GIZ (2015).

<sup>74</sup> Customer satisfaction surveys showed appreciation of improvements to cadastral and land registry services among private users, banks and notaries. It also showed that more people started seeing the value of clarifying or registering their ownership title. State data. LRP (2012).

<sup>75</sup> World Bank (2012), *LRP final report*, p.28.

<sup>76</sup> “By the end of March 2012, a total of 60,349 mortgages were registered in the Electronically Maintained Land Registry. 45.3 percent of these were transferred from the old books, while 46.4 percent were newly submitted and registered requests for registration of mortgages. The remaining 8.3 percent were the mortgages taken over from the Real Estate Cadastre.” World Bank (2012), *LRP final report*, p.36.

Thirdly, Ashdown's law was game-changing because governing elites no longer resisted the process of clarifying land records—in fact they supported it. The legislative intransigence that had characterized the period before Ashdown's imposition—like the earlier resistance to restitution—had been broken.<sup>77</sup> This might seem paradoxical, as the law might endanger their strong political influence on land exchanges: the new system would gradually permit indiscriminate public access to formal land exchange services. This meant registering real estate had become a more impersonal and less informal process.<sup>78</sup> But it did not mean that real estate investment was now devoid of politics or market distortions: obtaining other regulatory permissions (urban planning, construction permissions, procurement contracts etc.) was a slow process<sup>79</sup> that typically required political facilitation.<sup>80</sup> Yet what the process of clarifying land records did do was create a basis for formal real estate investment. After all, banks and foreign investors expected to see a proof of ownership from the land registries. The process thus enabled lucrative land improvements and other turnkey projects that were very difficult, if not impossible to attract before Ashdown's law. Not coincidentally, the real estate 'boom' that started in Sarajevo took off after 2002, after the adoption of Ashdown's law.<sup>81</sup> The first multi-billion euro opportunity to present itself was already 2003 (soon after Ashdown's law was adopted): the European Commission announced its South-East European transportation artery would run north from the Croatian coast past Sarajevo into RS to the Croatian hinterland.<sup>82</sup> A precondition to make this great font of investments (notably construction, material and transportation contracts) happen and to find willing

<sup>77</sup> The CRPC closed in 2003, its mission considered largely complete. *CRPC* (2004).

<sup>78</sup> From 2003 to 2006, LAP prioritized re-training land clerks. The rebalancing of responsibilities, as well as “decades without a single seminar” meant that too few clerks were trained, tested and licensed to deal with real estate disputes. The LAP thus invested in “on the job training” of 150 existing clerks and 250 new lawyers. *GIZ* (2015), pp.2-3.

<sup>79</sup> The World Bank noted in 2012 “The entities need to work to reduce market distortions, encourage greater investment and growth by improving the quality of the data held in the registers, harmonize the entries and address the problems of illegal construction and idle land. Illegal properties are still not selling as they cannot be easily registered in the land book due to missing construction permit.” World Bank Real Estate Registration Project Appraisal (2012), p.36.

<sup>80</sup> See Z. Moses, *Neo-Liberalism, the Islamic Revival, and Urban Development in Post-War, Post-Socialist Sarajevo*. M.A. thesis, University of Toronto (2012).

<sup>81</sup> M. Fischer, *Peacebuilding and Civil Society in Bosnia and Herzegovina: Ten Years After Dayton* (2004), p.95.

<sup>82</sup> A feasibility study estimated the highway to be around 1.5 billion euros. European Commission, *REBIS STUDY* (2004).

investors<sup>83</sup> was to clarify ownership about the land along the highway route.<sup>84</sup>

## Challenging and Adapting “Ashdown’s Law”

Despite the fact that the heavily decentralized system for recording and updating land titles was clearly becoming more functional thanks to horizontal coordination and cooperation between the courts and geodetic authorities, tensions about the implementation Ashdown’s land registration law resurfaced. At first glance this appeared mainly a result of “friction between the entity governments and GIZ.” The World Bank did directly disburse credit to the geodetic authorities, whereas GIZ did not. As GIZ was unwilling to change its disbursement policies, GIZ decided to end its 9-year old project in 2011<sup>85</sup> (even as a new five-year World Bank loan worth 34 million USD for a Real Estate Registration Project (RERP) was in the making (it was approved in May 2012)<sup>86</sup>). However, a more problematic, underlying issue, was a “frozen conflict” between lawyers and geodetic experts over the separation of powers in land registration. This existed since Ashdown imposed the Law on Land Registry. “Ashdown’s Law” evidently never achieved full acceptance, especially among officials in the geodetic administrations.<sup>87</sup> Meanwhile, GIZ’s support for building country-wide legislative coordination had self-admittedly not succeeded as “the political economy in BiH” began to “to emphasize more the Entity level authority.”<sup>88</sup> Entities were looking to centralize powers over land

<sup>83</sup> E. Jansson, (2004), PM turns on the pressure in big drive for new motorway, *Financial Times*.

<sup>84</sup> Z. Bačić and V. Poslončec-Petrić, *Regional study on cadastre and spatial data infrastructure* (2012), p.105.

<sup>85</sup> According to GIZ this made the donor recipients feel “capable of implementing activities without the technical assistance of LAP [GIZ]” and subsequently, “[t]he LAP was increasingly perceived as a project with the objective of supporting the WB [World Bank] project, which meant that it should only fund the necessary human resources to strengthen their own teams and provide additional financial resources to supplement the WB loan. This approach was not acceptable to the LAP donors, [...] [and] an exit strategy was jointly agreed.” GIZ (2015), p.23.

<sup>86</sup> That project, again with Federation and RS ministries of justice as beneficiaries would seek to sustain and enhance progress with more infrastructural and policy development and seek to harmonise land registries and cadastral records in urban areas. World Bank Real Estate Registration Project Appraisal (2012), p.36.

<sup>87</sup> GIZ (2015) p.23.

<sup>88</sup> A designated state-level coordination body (the Land Administration Coordination and Advisory Board (LACAB) had failed to live up to its task of proposing “appropriate” measures to improve the land registration system: slow government formation at the Fed-

registration under the geodetic authorities and away from the more independent court presidents. The old debate over centralization or separation also divided GIZ and the World Bank, who evidently could not agree on a common response.<sup>89</sup> While GIZ claimed neutrality, it thought the World Bank was biased towards centralization.<sup>90</sup>

In February 2011, soon after GIZ left (and the era of Ashdown and OHR interventionism was long over), the RS parliamentary assembly adopted a new Law on Cadastre. This law was similar to Ashdown's law in that it re-unified the previously separated cadastre and land registry under RS' geodetic authority (RSGA). The RSGA argued centralization would expedite harmonization of the cadastral and land record data.<sup>91</sup> Yet for GIZ, the RS law "could be considered a major setback for the efforts undertaken by the LAP" as

Choosing between a "dual" or "single" administrative solution for managing the land registry and cadaster is not important, a clear separation and the strong coordination of legal and geodetic functions is in any case "a must"<sup>92</sup>

In other words, it was feared that the registration of property rights—real estate—the land registry should have remained administratively separated to ensure the registration of land records at the RS' geodetic administration would not come under direct political influence.

This fear was shared by Bakir Izetbegović, the Bosniak president, who suspected the centralized system could be abused to enable unlawful land reallocations of real estate abandoned by refugees or left vacant during the war. Without the appropriate checks and balances, outdated land

---

eration and State level impeded formulation of nation-wide strategic guidelines. *GIZ* (2015) pp.25-26.

<sup>89</sup> According to the leader of the Bosniak caucus in the RS Assembly, Mujo Hadziomerovic "The Council of Ministers of BiH, and part of the international community hesitate(d) and said—reach agreement among yourselves"—suggesting that this created a window of opportunity for this reform. *Bosnia Daily*, *Bosniaks Veto Republika Srpska's Law on Cadastre* (2011).

<sup>90</sup> GIZ, after its departure essentially blamed the World Bank for taking sides in the "frozen conflict" between lawyers and cadastral officials had endured, which was "aggravated by the advent of donors who promoted the unification of the cadastre and land registry under one authority." *GIZ* (2015) p.23.

<sup>91</sup> Interview, Tamara Travar, Deputy Project Coordinator, Real Estate Registration Project, Republic Authority for geodetic and property affairs of Republika Srpska, Banja Luka, November 4, 2015.

<sup>92</sup> *GIZ* (2015) p.23.

records could be altered without proper due process: e.g. by changing land ownership titles without consultation of absentee owners who might someday return to formally clarify their ownership rights and/or return to their property. Izetbegović thus challenged the law in the constitutional court, and this eventually brought RS to amend the law.<sup>93</sup>

Since then, the World Bank worked with the geodetic authorities to develop and implement regulatory safeguards to avoid geodetic authorities in the RS and FBiH abuse to reallocate unclarified land without due process.<sup>94</sup> The FBiH government followed the RS and proposed a law to centralize land registration powers, which by early 2016 it had not yet adopted. Meanwhile, the idea of centralizing land registration power persevered: At a World Bank conference in 2016, the Directors of both entities' geodetic authorities jointly stated that "the transition of the dual registration system into a single, unified one is internationally recognized as a best practice."<sup>95</sup>

## Analysis of the Bosnian Land Registration Reform

How do these findings answer the research questions? What hypotheses can be confirmed? Some evidence presented above gives reason to argue that land registration reform was driven by Ashdown's move to impose a preconceived solution (reinstating the two-book system). His leadership was arguably "indispensable" in changing the rules of the game. His aim was to create an institutional framework and to clarify responsibilities (between entity geodetic authorities and the court's land registry offices). This framework was the basis for implementation and donor support. Further, it quashed domestic legislative intransigence and disagreements. Finally, the improvements in the Doing Business Index and specific project performance indicators suggests the reform approximated "international

---

<sup>93</sup> Constitutional Court BiH, Decision on Termination of Proceedings regarding review of the constitutionality of the Law on Cadastre of the Republika Srpska (*Official Gazette of Republika Srpska* no. 60/11 (2012))

<sup>94</sup> Interview, Sarajevo October 14, 2015; November 30, 2015.

<sup>95</sup> Like RS, the FBiH said that the unification of the cadastre and land registries would make it "easier" harmonise and to collect real estate data. Moreover, a survey submitted to The World Bank indicated that notaries and surveyors were complaining about the inefficiency of the Federation's property registration system. At a World Bank land governance conference in 2016, the director of the Federation geodetic authority, Mr. Obradović, maintained that a unified land information system was international "best practice" and a goal. See Obradović et. al. (2016)

standards”—even increasing real estate market activity—and conceivably advanced the country towards an open access order. In short, key evidence can be used to confirm part of the hypotheses of the solution and leadership-driven change (SLDC)-theory of reform (H1-4—see table 1).

However—a deeper reading of the presented evidence suggests this case typifies problem-driven iterative adaptation (PDIA). Firstly, Ashdown’s law was not a comprehensive or permanent solution; it was the starting point for the search for one, and marked the acceptance of a deep-rooted and evolving problem: the legacies of socialism and war had made land records extremely unreliable. Only four years after Dayton, when the failure to implement restitution was connected to failure to attract foreign investment, did land registration reform become a priority for the international community, i.e., the PIC. The PIC recognized unclear land records as both an obstacle for restitution and the country’s ability to attract investment. It subsequently expected domestic legislators to concoct a reform that would allow for a systematic process of clarifying un-harmonized land records (and land registration procedures). Yet domestic lawmakers remained in disagreement over this reform. After two years of fruitless attempts to pass a law, High Representative Ashdown’s fear of an imminent economic crisis led to the imposition of the Law On Land Registry. This law clarified the legal framework and institutional responsibilities yet lacked a plan. Thus H5 (not H1) can be confirmed (see table 1). As for who drove implementation: there was not one actor leading implementation: rather a coalition of domestic actors and donors began finding and fitting solutions iteratively, incrementally and adaptively. Each actor played a different role, which changed over time. This is well illustrated in the case study. Domestic elites adapted by ending their erstwhile political intransigence upon realizing their political and economic interests were served by seeing this reform implemented (namely because ownership clarification opened opportunities for attracting investment and large-scale real estate projects.) The World Bank adapted by *de facto* accepting the revisions of Ashdown’s law and recentralizing land registration powers in the RS. By contrast, GIZ had difficulty adapting, and eventually left. As the entities and the World Bank continued to agree that the main aim was to make land registration more functional: centralized authority in exchange for ever increasing harmonization of land records and registration systems in Bosnia and Herzegovina was acceptable to all key stakeholders involved.

In short, the continued search for context-appropriate solutions and institutional adaptation is what made possible the land registry law and continued political, financial and technical support to enhance land registration functionality in BiH. Domestic acceptance of the need for retraining, modernization and standardization of local land registration capacities was as important as the World Bank's acceptance of the local desire to recentralize separation of land registration powers. Evidently, the World Bank wagered that centralization would not undermine their project performance indicators.

Facilitating access to land registration services and clear records appears to be an advance toward an open access order—just as the improved Doing Business Score for the ease of the registering property suggested. Yet this was a result of an approach that did not involve straightjacketing according to predefined standards, and left room for external and internal ideas to adapt the reform after it was adopted and being implemented.

## Conclusions

Three conclusions can be drawn from this analysis. Firstly, the unbroken political support for land registration reform since 2002 suggests the surprising possibilities of PDIA. The reform made Bosnia and Herzegovina more akin to an open access order. This analysis shows powerful actors, like the High Representative, playing a surprisingly modest role in enabling this outcome, which is perhaps not expected may at first glance. The case study finds that the reform moved ahead more because involved actors, motivated by enhancing the country's ability to attract greater investment, continuously adapted to new roles and situations to drive change toward a more competitive and transparent economy. In a country where political compromise over comparable economic reform often has been considered problematic, if not impossible, this finding seems remarkable.

Secondly, the analysis shows the limits of PDIA. Governing elites did not block the process of enabling greater transparency about who owns what land by clarifying land records, yet they did move to remove the courts' role as an immediate check and balances to prevent potential abuse of the power to regulate land records. Meanwhile, political elites successfully undermined institutional capacity that would clarify their own real estate records, and thus kept potential conflicts of hidden interests.<sup>96</sup>

---

<sup>96</sup> Group of States Against Corruption, Second Evaluation Round Report, *Compliance Report on Bosnia and Herzegovina*, Council of Europe (2008); European Commission, *Progress report*

Moreover, attempts to link land registration with property taxation systems were only beginning at the time of writing this paper.<sup>97</sup> It is unclear if further attempts in enhancing the functionality of land registration will remain contingent on backtracking or lack of change in areas directly related to land registration.

Finally, the possibilities and limits of PDIA suggested in Bosnia and Herzegovina raises further questions. PDIA in this case shows external donors and domestic actors finding compromise after confrontation, but political acceptance by the governing elites appears to be a pre-requisite for change. Is this really the case? If donors lack clear or complete standards on checks and balances in land registration<sup>98</sup>; is that helpful to advance liberalizing institutional reforms, or is it a shortcoming that elevates the abuse of institutional power for narrow political and economic ends? Secondly, if only a narrow elite is able to take advantage of the new economic opportunities a reform (here land registration reform) creates (as research on land registration reform in Cambodia suggests) does this not affect the legitimacy of donors supporting land registration reform?<sup>99</sup> Thus while this chapter may provide insights why and how PDIA may drive and overcome obstacles to reforms that governing elites and donors promise will open up the economy to competition and investment—it does not verify if this promise is actually fully delivered. Hopefully this will stimulate researchers and policy-makers to think about and critically evaluate the adoption and implementation of comparable reforms in Bosnia and Herzegovina and other post-conflict countries.

---

*Bosnia and Herzegovina* (2010), p. 15. Interview, Leila Bicakčić, Director of the Center for Investigative Reporting (CIN), *Center for Investigative Reporting (CIN)*, December 11, 2015.

<sup>97</sup> Z. Obradović et. al. Building Capacity and Communication for Land Administration in BiH, *Annual World Bank Conference on Land and Poverty*, Washington D.C (2014).

<sup>98</sup> The donors who continued to monitor progress on land registration reform, namely the World Bank (and also the EU) remain watchful on improvements of the DBI score, yet indifferent to particular aspects. A clear illustration is their position on centralization of land registration powers. From what can be told from the EU ‘progress reports’ the EU remained indifferent whether centralization heightened the risk of abuse of land registration powers (as mentioned, it lacks a clear *acquis* on the point). The World Bank appears to simply recognize that for a long-running land registration project creating a uniform, integrated land registration system is becoming a norm globally (thus contrary to entities’ claims, the World Bank nor any other donor has an explicit standard for whether land registration powers should be centralized or separated): “The World Bank, too, has exhibited [...] the assumption that one uniform set of land laws based on a Western model would facilitate foreign investment in land” However, he noted that “There is a growing recognition that rather than attempting to impose a uniform national land law in such countries, an approach that recognizes the strengths and benefits of diversity is more likely to encourage social stability and economic development” Deiniger et. al. (2010), pp.155-156.

<sup>99</sup> Biddulph (2014).



*Part II*

**Institutional and Political Reforms**



## *Chapter 7*

# **How to Reform the “Reformers”?**

*Srdjan Blagovčanin*

There is a well-known and often-cited Darendorf maxim that states it takes six months to formally replace a political system, six years to transform an economic system, and 60 years to bring about social change that establishes a participatory political culture and civil society. After more than twenty years, it seems that Bosnia and Herzegovina (BiH) has not advanced much in instituting changes that lead to a participatory and democratic political culture, and as a consequence, economic transition has remained trapped in a limbo of populist-clientelism. Foucault’s interpretation of the famous Clausewitz dictum “politics as the continuation of war by other means” best reflects the situation in BiH, almost twenty years since the state-building process was started. The reforms that were implemented have proved unsustainable, whereas the power vacuum created after the international community pulled out of the operational management of the country was quickly filled by kleptocratic ethno-political elites driven exclusively by their own interests.

There is an almost general consensus to be found among pundits familiar with the situation in BiH and in the findings of various studies, which states that the democratic, EU-oriented reforms in BiH have been reduced to a mere form, with the majority of its citizens effectively excluded from decision-making processes. While the vast majority of citizens have continuously expressed their support for the country’s membership in the EU, the very few options available for influencing the decision-making process have prevented them from exerting any significant influence on political elites.

The relatively low electoral turnout, decision-making processes that take place away from the public eye, and decisions adopted in urgent parliamentary passage procedures in half-empty assembly halls, are but symptoms of a dysfunctional democracy. The recent developments surrounding the adoption of laws envisaged under the Reform Agenda are just the latest in a series of caricature examples of how reforms are approached in the country.

If one is to understand the political dynamics of the country, it is necessary to bear in mind the very structure of these political elites as key actors. The current political elite in the country emerged in the early 1990s, with the introduction of a multiparty system in BiH. A considerable portion of this political elite was formed during the war and post-war ethnic strife, a period that was marked by utter chaos and an absence of the rule of law. This allowed the elites to amass enormous wealth through direct budget transfers, black-marketsteering, and illegal privatization of state property.

In this regard, it is important to note a relatively new form of corruption, namely “state capture,” which occurs together with the process of transition and is conceptually defined precisely on the examples of East- and South-east European countries. The state capture phenomenon differs from corruption in a key feature: “While most types of corruption are directed toward changing how existing laws, rules, or regulations are implemented with respect to the bribe payer, state capture refers to corrupt efforts to influence how those laws, rules, and regulations are formed.”<sup>1</sup>

This particular form of corruption is exactly what occurred following the collapse of what was a strong socialist country with robust centralized institutions, when emerging actors used the power vacuum to form new rules for their own benefit. These ethno-political elites, emerging immediately before and during the armed conflict in BiH, and amassing enormous amounts of wealth by controlling the movement of strategic resources, would ultimately become the key actors in the process of state capture.

If we analyze this further, we can easily identify political parties as one of the key generators of this situation. The absence of minimal democratic standards within political parties resulted in a situation where such undemocratic party practices are replicated in state institutions. If parties are internally undemocratic and operate with the primary intention of seizing treasures in the form of public resources, which are then shared among the party leaders and membership, it results in a replication of the same model in state institutions. The hypertrophied power and influence of political parties has also hindered the development of a classic tripartite separation of power into legislative, executive and judicial branches. The institutions remain mere shells, while the real power is concentrated in

---

<sup>1</sup> Joel Hellman and Daniel Kaufmann, “Confronting the Challenge of State Capture in Transition Economies,” *Finance and Development*, September 2001, Volume 38, Number 3, p. 2. <https://www.imf.org/external/pubs/ft/fandd/2001/09/hellman.htm>.

the hands of a few political leaders who, through clientelism, ensure effective control over all three branches of government.

This has led to a situation where the public sector, instead of being subjected to radical reforms, became an end in itself, continuing to grow abnormally, incessantly creating new administrative procedures and giving large and uncontrolled discretionary powers to all levels of government. This has created new opportunities for corruption.

A huge portion of GDP is distributed through various administrative levels (over 50 percent of GDP), without basic transparency, and without citizen participation in decision-making processes, completely subverting the order of priorities and placing the public interest well below the interests of a narrow circle of ethno-political oligarchy. When comparing the level of public spending across Western Balkan (WB) countries, only Serbia is at the same level as Bosnia and Herzegovina, while the level of public spending in other WB countries is significantly lower.<sup>2</sup>

If we look at the phenomenon of state capture as a closed circuit, the influence of political elites and powerful oligarchs is manifested in the adoption of laws that suit their own interests, while political influence and administrative corruption have prevented law enforcement agencies from identifying and prosecuting illegal activities. Furthermore, political influence on the judiciary hampers the prosecution of major corruption cases, and the media completes this vicious circle as a tool for numbing the public and presenting a completely distorted list of social priorities.

In this regard, one has to keep in mind that the primary interest of the omnipotent political pseudo-elites is only to maintain the status quo. Any change threatens their unlimited power, exposing them to the risk of criminal prosecution.

As for the conditions and initiatives stemming from the EU, political pseudo-elites in BiH have learned their lessons. They go through the motions and simulate reforms long enough until the EU comes up with a new initiative or agenda, completely forgetting the previous requirements. The examples are numerous, ranging from the reform of the police, constitution, public administration, to the reform of the judiciary. In the vast majority of those reform processes, the pattern has largely been the same—after endless discussions and under strong pressure from the inter-

---

<sup>2</sup> *Public Expenditure and Institutional Review (PEIR) for Bosnia and Herzegovina*, World Bank, February 28, 2012.

national community, even if a consensus on adoption of reform legislation has been reached, the implementation of this legislation is thwarted by the failure to secure necessary budget funds or by the inability to agree on the appointment of the management, i.e. establishment of political control over the institution. Such was the case with the police reform and the establishment of state police institutions, as it was with provision of funds for the functioning of the state judiciary, the establishment of the state-level anti-corruption agency, etc.

Transformation of this specific “captured” political system is by no means easy, but it is a prerequisite for sustainable reforms, ranging from the economy and education system, to the rule of law. Since the key problem is at the political level, solutions are needed on the same level and have to entail key actors in political system: political parties and political elites. The change of this situation implies that the political parties and elites would need to relinquish their accumulated power and acquired resources, i.e., agree to a different division of powers in favor of the silent and apathetic majority who does not vote or participate in elections. Something like that has, of course, never and nowhere happened as a result of the good will of political parties or leaders and without strong pressure from the silent majority, and it will most certainly not happen here either.

A process that would lead to this kind of change should include changes that would unfold in two directions: the introduction of internal party democracy, and the introduction of compulsory voting.

The introduction of basic intraparty democracy standards, is the first step in breaking ossified structures and clientelism in political parties which operate with the sole interest of dividing resources among their membership. To change the current political logic and dynamics, it is necessary to introduce a “one member—one vote” principle in the election of party leadership and selection of candidates to electoral lists. The way in which political parties currently operate, where leaders elect delegates at the party congress and these in turn vote for them so that they can later be included in the electoral list or be given a sinecure in a public institution or enterprise, only perpetuates the clientelism and the fundamentally undemocratic practices of political parties and, by extension, the entire political system. Therefore, the introduction of a legal obligation for political parties to introduce intraparty democracy would be an important step forward.

The second direction of change—introducing compulsory voting—would be twice as important. This step would undoubtedly lead to increased citizen participation in decision-making. Furthermore, it would contribute to greater accountability of political parties to voters. Instead of using anachronistic methods of wooing voters who rely on benefits from the public administration (through a job in the public sector or other sinecures), this change would mean that political parties would have to appeal to a far broader range of potential voters as well as offer much better political programs if they want to win their support.

Studies done in countries where such a system is in place have reported undoubted positive democratization trends. Although the system currently exists in only 22 countries, debates about its introduction are increasingly gaining traction.<sup>3</sup>

The current power relations in BiH’s political system are reminiscent of a hostage crisis, where the ruling elite uses accumulated powers to keep hold of all the levers of control over state institutions and resources, completely excluding the public and civil society from decision-making. The feigning of reforms and fulfilment of EU conditions has reached perfection.

Given the ruling pseudo-elite’s interest in maintaining the status quo, i.e., maintaining unlimited power and control over public resources and institutions, the impetus for this type of process in the form of conditions and requirements would have to come from the outside, primarily from the EU. No matter how discontented the silent majority is, their demands for change have been deftly blocked by the ruling pseudo-elites through methods of manipulation and deception aimed at drawing attention to ethnically homogenizing themes, and the overt use of force.

---

<sup>3</sup> There are many advocates for instituting compulsory voting, including well-known scientists like Arend Lijphart.



## *Chapter 8*

# **The Reform Agenda and Beyond: Transitional and Structural Reforms for the New Generation of Bosnia and Herzegovina**

*Adis Arapović and Adisa Omerbegović*

Bosnia and Herzegovina, a country in southeastern Europe with a thousand-year turbulent history, builds its modernity under many burdens of the distant and near past. The nation's culture has been marked by the 415 years of feudal Ottoman-Turkey rule (1463–1878) and afterwards, by the 40 year-rule of a hybrid Austro-Hungarian (1878–1918) occupation. The authoritarian Yugoslav monarchy (1919–41), as well as the totalitarian communist dictatorship (1945–91) have significantly derogated the social substance abilities for a timely modernization. An almost uninterrupted series of 550 years of foreign authoritarian and/or totalitarian rule with unfinished nation-forming have reduced the possibility for a quick transitional success after the fall of communism and the dissolution of socialist Yugoslavia in the early 1990s. Instead of a transformation modeled after other countries of the Eastern bloc, the first stage of transitional modernism in Bosnia and Herzegovina was marked by a brutal perennial war (1992–95) with elements of aggression from neighboring countries, and an internal civil war which NATO ended by intervening after 200,000 fallen victims, over a million refugees, and a committed genocide. Following this, the Dayton Peace Agreement and a new constitution came to life.

The new constitutional solution established a very complex and asymmetric institutional structure with two equal entities: a decentralized Federation of Bosnia and Herzegovina (FBiH) (51 percent of BiH territory with a Bosnian and Croat ethnic majority), comprised of 10 cantons for which the federal level shares almost all prerogative authorities, and a second, centralized entity—Republika Srpska (RS) (with a Serb ethnic majority), with prerogatives on the entity level. The highest, national level of government, with a complex composition and mechanisms of decision-making in a bicameral parliament, a tripartite rotating Presidency and a Council of Ministers established on a partite ethnic filling and decision-

making. The national level has significantly reduced jurisdictions, a very complex and long decision-making process, and possibilities of veto blockades from the lower levels of government, ethnic parliamentary clubs, mono-ethnic parliamentary parties, and even from individuals in the highest executive positions.

The first post-war decade (1996–2006) was marked by visible reconstruction, political and economic consolidation, as well as a slow but present inter-ethnic reconciliation. In this period, international presence in BiH, in the form of the Office of Higher Representatives (OHR), ensured a national continuity, institutional and legal reconstruction, as well as starting up postponed, but basic transitional reforms—primarily legal-political and economic ones. It is worth noting the success of the reforms and unification of the military, establishing dozens of new institutions, a tax system, conducting the first wave of (controversial) privatizations, holding legitimate elections, etc., yet all of this with the OHR often in the role of lawmaker.

However, after 2006, largely due to the failure of some structural reforms (most notably the reforming of the constitution), the OHR started to shift its action and decision-making strategy to be completely left to the local institutions and political actors, which produced eight years of almost complete political and economic stagnation, frequent blockages, and internal political crises. Combined with the global recession, in the period 2008–14, the economy recorded serious falls, very low investments, and unemployment and social inequality that were not only an economic, but also a political problem.

In early 2014, mass street protests erupted, and citizens violently expressed their dissatisfaction with the social, economic and political situation in the country. The tripartite ethnic division of the government, media and public opinion, the political manipulation and particular interests of individuals, groups and political parties, trumped general interests and the necessity of reforms and opportunities for prosperity, which threatened this social unrest to explode into a political and inter-ethnic confrontation.

### **Reform Agenda: Genesis**

Directly after these unfortunate events, at the initiative of the Office of the EU Special Representative in Bosnia and Herzegovina (EUSR),

with an active role of the World Bank (WB) and International Monetary Fund (IMF), the “Compact for Growth and Jobs” was created from a set of recommendations from the so-called “Forum for prosperity and employment.” This forum brought together a group of representatives from domestic institutions, civil society, and the international community in Bosnia and Herzegovina (BiH) with the common aim of achieving a consensus on the necessary reforms in several areas of public policy.

The inauguration of the diplomatic project called “The British—German Initiative,” in late 2014 after the general elections in BiH, later to become the initiative of the European Union (EU), placed BiH on the fast track towards EU candidate status. Certain political conditions for unblocking the euro-integrational process ceased to be predominant, and the level of readiness of the local political authorities to implement primarily economic reforms was established as a causal instrument of EU integration, as well as a condition for the support of the international community for the transition reforms in BiH.

The Compact for Growth, a conceptual framework of reforms needed in order to significantly stabilize social conditions, enhance economic growth and development, and improve the standard of living, was a prelude to the initiation of a comprehensive package of reforms passed at the beginning of 2015, called the *Declaration of the Presidency of Bosnia and Herzegovina*. This initiative was publicly supported by the signatures of 14 parliamentary party leaders. Further clarification of the provisions of the Statement in measures of public policy were made in the document “Reform Agenda for Bosnia and Herzegovina 2015 to 2018,” which was officially passed by the Council of Ministers and entity governments in the period July–September 2015. Governments committed to the imperatives and objectives of the Agenda to be translated into action plans. Between August–October 2015, the BiH Action Plan was passed, and the Federation of BiH (FBiH), the Republic of Srpska (RS), and subsequently all cantonal authorities in FBiH started developing and implementing their own Action Plans.

The purpose of the Action Plans was to ensure, through concrete legislative and other measures, the implementation of the principles and objectives contained in the Reform Agenda, with the aim of stopping the economic downturn, starting the process of rehabilitation and modernization of the economy, fostering sustainable, efficient, socially just and balanced economic development, reducing public consumption, primarily overpriced and inefficient administrative apparatus, job creation, improve-

ment and proper routing of social protection, the creation of a favorable and equitable social environment, and, perhaps most importantly, strengthening the rule of law, and introducing zero tolerance of corruption.

Why is the Reform Agenda so important? The Reform Agenda, despite being the overarching opinion of the general public on internal inconsistencies and the “wish list” syndrome, is much deeper and has a much wider framework than mere economic-social reforms. The principles and objectives of the Reform Agenda interfere with the ideological values, historical heritage, and political beliefs of those who govern and those who are governed. Therefore, it is important to track, measure, prove, improve and accelerate the transition, mentality and cultural reforms that BiH citizens and the society as a whole, even after 25 years of transition—have not yet gone through. After 10 years of stagnation, an absence of legal, political, economic and other reforms, and a very sluggish and often blocked process of EU integration, the Reform Agenda is for many players from the EU, but also from Bosnia, perhaps the last great opportunity to overcome disintegrating vectors, and to step aboard the high-speed train towards full EU membership, and ultimately, to allow its citizens and future generations for a dignified, secure and prosperous life.

### **A Turbulent 2016: Unplanned Aggravating Circumstances**

At the time of the finalization of this article, the situation in Bosnia is a multi-controversial, complex and unpredictable one. On the other hand, a year and a half after the inauguration of the Reform Agenda and a year of very active work on implementing the action plans, there are several reasons for optimism.

Some reforms that have been delayed more than a decade are finally launched, such as a new labor legislation, reform of the pension system, and the simplifying of procedures for starting a business. Also, some economic indicators such as GDP growth, export growth and industrial production, and the number of employees, even though not drastic, recorded significant growth compared to the previous year.

It is indicative that the European Union accepted the application for full membership of Bosnia and Herzegovina into the EU in September 2016, recognizing the credible progress in the implementation of the Reform Agenda. This is the first step in a long and complex accession process. It is expected that the European Commission Delegation will

soon deliver a comprehensive questionnaire to local authorities to assess BiH's suitability for EU membership. The status of a potential candidate, as a feature of Bosnia for ten years, will therefore remain at least a year in force, by which Bosnia remains on the list as a secondary priority of EU enlargement policy, as opposed to all the neighboring countries which do have candidate status and open negotiations with the EU—Serbia, Montenegro, Macedonia, and Albania.

The acceptance of the application for candidate status is so far the biggest step towards EU membership. Even though the acceptance of the application was preceded by several important internal compromises (coordination mechanism of decision-making in the EU accession process at the national level, the publication of the census results, the revised trade agreement with the EU), internally, this plan did not contribute to political stabilization and the focusing on reforms and objectives arising from the application for membership. On the contrary, RS failed to recognize integrated census results, and instead published their own census several months before the local elections on February 10, 2016, which instigated a harsh political crisis.

At the same time, the entities' authorities refused to implement the decision of the Constitutional Court on the unconstitutionality of a holiday—the so-called Republika Srpska Day, and have now scheduled a referendum on the decision of the Court. The referendum itself was declared by the Constitutional Court as an unconstitutional action and ordered its banning. The entity authorities ignored this, and a week before the local elections, they held a referendum. The election resulted in favor of the nationalist parties in both entities, which we can largely attribute to the preceding referendum. The international community of BiH, including the EU Delegation, the EU diplomatic presence in the country, the US Embassy, OSCE, Council of Europe, and others, with the exception of Russia, pointed to a breaching of the rule of law, institutional order, the Constitution, and thus the Dayton Peace Agreement. The political debate on the referendum led to tensions between political actors, not only in BiH, but also in the region. For the first time in 20 years of public discourse, threats of a new war were uttered, and the RS government voiced intentions to call for referendums on other matters outside their jurisdiction, including a referendum on its secession from Bosnia and Herzegovina.

Such rhetoric and obvious unconstitutional action have produced quite aggressive reactions in the other entity, as well as calls from the OHR to punish violators with the highest legal means (because only the OHR has

this authority) disable the anti-constitutional precedent, and ensure the protection of the Constitution and the Dayton Peace Agreement. The OHR was unable to reach consensus after 60 days of the referendum, due to the widely different opinions of members of the Council for Peace Implementation Council (PIC), the supervisory authority of the OHR. It should be noted that several judges of the Constitutional Court had political careers in the current ruling political parties, which nominated them for these positions.

In addition to the negation of this order, there are 90 other verdicts, which have been either partially implemented or not implemented at all. One of the verdicts instructed the Bosnian authorities to ensure the implementation of the local elections in the City of Mostar without discriminatory provisions in the Statute, which the Constitutional Court revoked in 2011. Due to this, Mostar's inhabitants are unable to choose local authorities for the past two election cycles, and for the fifth year in a row, they do not have representatives in the local parliament. This is just one event that has marked the recent local elections and the overall political discourse of 2016.

## **The Successes and Failures of the Reform Agenda**

What effect could the Reform Agenda possibly have in this contaminated political context? To understand the success and failure of the previous implementation of the Reform Agenda, we need to understand the structure, objectives and expected outcomes.

The reform agenda outlines precise medium-term priorities divided into six areas of public policy:

1. Public Finance, Taxation and fiscal sustainability;
2. Business climate and competitiveness;
3. Labor Market;
4. Reform of the social security and pensions;
5. Rule of law and good governance;
6. Reform of the public administration.

The agenda places a priority on the public finances for all levels of government, as these have been very weak for many years. It is necessary to implement fiscal consolidation, which will then gradually lead to a reduction of the budget deficit and public debt levels. In order to amortize the

pressure on the monetary and financial system and the fiscal disorder that will inevitably happen with implementing these reforms, a new loan agreement worth 560 million dollars, was signed with the IMF in September 2016, while additional financial support is also expected from the World Bank and the European Commission.

As stated in the Reform Agenda, “Fiscal consolidation aims to ensure a stable macroeconomic environment, but for a stable, positive real growth in the medium and long term, it is necessary to implement a number of structural labor law, public administration, social benefit and employment policy reforms, improve the business climate and private sector competitiveness, restructure public enterprises, and increase the rule of law.”<sup>1</sup> Thus, there are strong causal links between the different areas of Agenda, so it is an understandable interpretation of equal importance and the need for parallel action in all fields simultaneously.

There are 170 short, medium, and long-term adopted action plan measures within the above-mentioned areas, which if implemented, would achieve the expected results. Before we provide a qualitative assessment of the implementation and effectiveness of the Reform Agenda, it is important to analyze the creation and implementation process.

The adoption process of the Reform Agenda, especially at the state and entity levels, was extremely non-transparent and one-sided. The action plans of the Council of Ministers and the RS government were not publicly available two months after the adoption, which further derogated the public trust in good and honest intentions of government. The action plans only became publicly available in December 2015.

A year and a half after its adoption, 46 percent of the Reform Agenda has been implemented at the BiH, FBiH and RS level, i.e., 79 out of 172 measures. More specifically, 52 percent of the planned measures (17 of 33) has been implemented at the state level, 36 percent (22 of 61), at the FBiH level, and 51 percent (40 of 78) at the RS level.

Important measures, such as primarily laws, were often adopted without a public hearing, contrary to the parliamentary procedure and public interest. In the FBiH, five out of eight (or 63 percent) of the adopted laws were done so on an expedited basis, in the RS there have been 18 adopted laws, of which nine have been adopted on an expedited basis, or 50 percent,

---

<sup>1</sup> Reform Agenda for Bosnia and Herzegovina 2015–2018, p. 2. <http://europa.ba/wp-content/uploads/2015/09/Reform-Agenda-BiH.pdf>

while at the state level legislation related to the Reform Agenda was not recorded on an expedited basis.

In early 2016, the non-procedural adoption of legislation was challenged in constitutional courts, and the Constitutional Court of the Federation of Bosnia and Herzegovina challenged the adoption of the new Labor Code, and ordered the FBiH Parliament re-enforcement procedures. Another difficult case was registered by the decision of the FBiH Constitutional Court, in June 2016, which repealed key provisions of the new Law on Civil Servants, disputed both on a procedural and a content basis.

Part of the laws passed in its content did not follow the principles and objectives of the Reform Agenda, and there are increasingly more objections to political parties or individuals in power using the Agenda for private interests. The best proof of this is the previously mentioned law on civil servants FBiH, challenged at the Constitutional Court, which would have provided an even higher level of politicization of public administration, political appointments of senior civil servants, without any criteria of merit, qualification and ranking, contrary to the imperatives of the Reform Agenda.

A quarter of the action plan measures is inestimable and not able to be monitored or analyzed as the general formulations usually represent a process, not a measurable outcome, and neither is limited by a deadline. Action plans at the state and entity levels predicted 26 percent of the measures for which the implementation period of time is “continuous.”

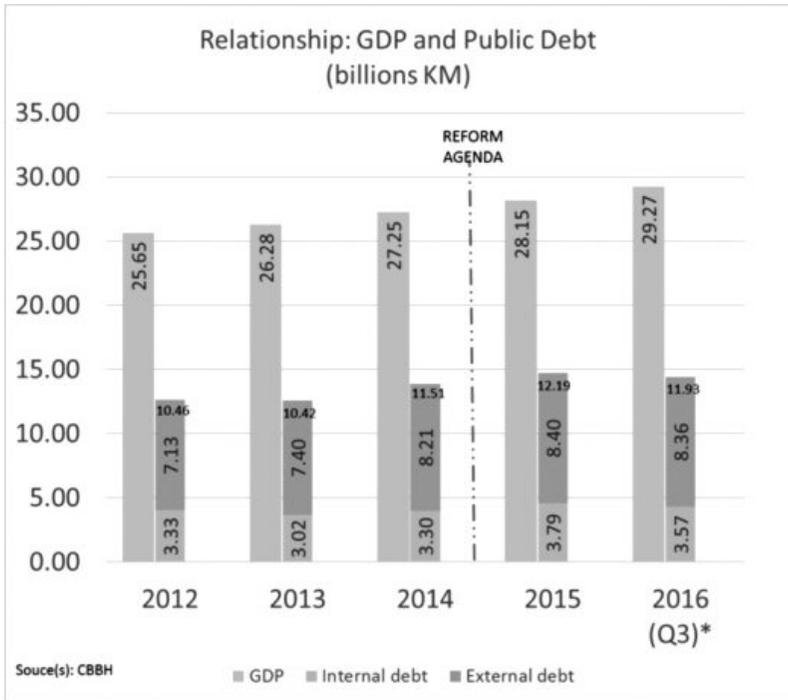
## **Section 1: Public Finance, Taxation and Fiscal Sustainability**

The objective of the Reform Agenda is to bring public debt to a declining path, and to create space for increasing public investment and at the same time reduce the government sector’s share in the economy. Fiscal consolidation should be implemented by reducing public spending and increasing public revenues. The increase in revenues will be achieved by raising the tax revenue, broadening the tax base, reducing the gray economy, reducing tax exemptions and improving the tax administration’s work.

Below we will present trends in several indicators for a few years, that is, the situation before and after the adoption of the Reform Agenda.

The total public debt has been growing for six years, reaching a historic maximum of 43 percent of GDP in 2015, where it increased by 30 percent

**Figure 1. GDP and public debt**

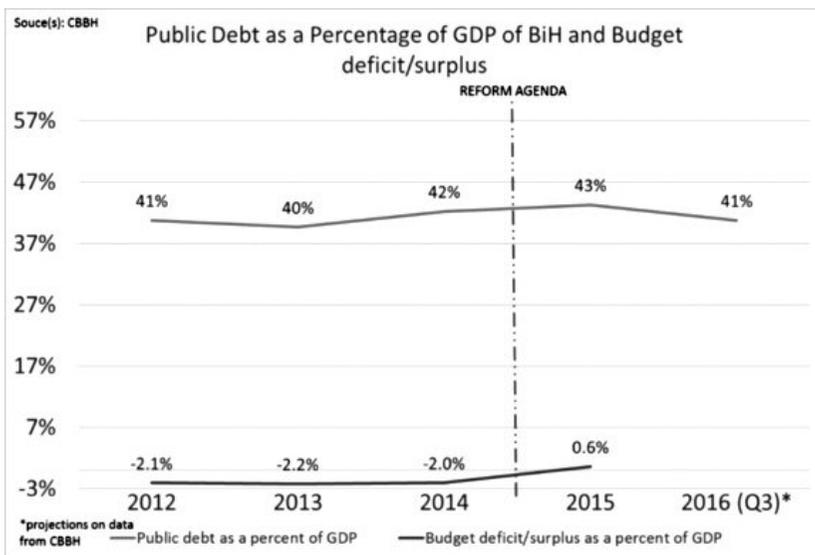


in the period from 2010 to 2015. This trend is unsustainable, and without a very serious approach to reforms, it will likely lead to extreme budget cuts, and extreme tax increases. In addition to borrowing from international financial institutions, which can even be considered as a stabilizing element, the majority of borrowing falls under unsustainable and expensive internal and commercial borrowing, which has multiple negative consequences.

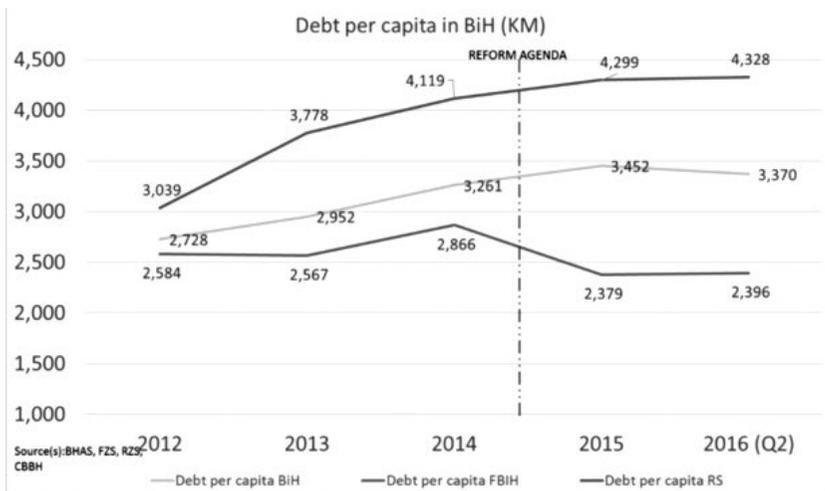
Figure 2 provides an overview of the public debt and budget deficit to GDP ratio during a period of six years, where we see progress over several years. These are also critically important macroeconomic indicators, since they are part of the EU (Maastricht) criteria. For the years 2015 and 2016, official data on the budget deficit has not been published, which is yet another example of the outdated and inefficient public statistics in BiH.

Debt per capita has seen a consistent increase until 2015, and now amounts to 3,370 BAM. During the six years measured (2010–2016), debt per capita increased by 911 BAM, or 37 percent, whereas the debt per

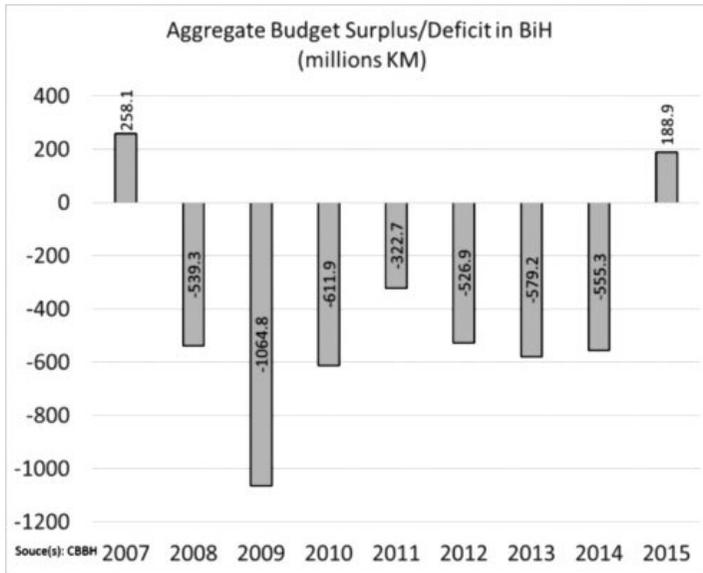
**Figure 2. The share of the public debt and budget deficit to GDP**



**Figure 3. Indebtedness per capita in Bosnia**



**Figure 4. The aggregate surplus / deficit in BiH**



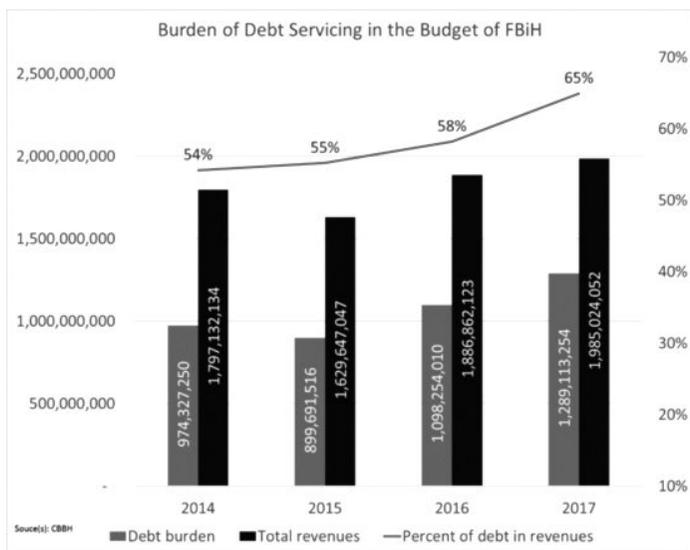
capita in the RS entity is higher by 180 percent compared to the F BiH entity. Indebtedness at the end of 2016 was significantly increased by the new tranche of credit arrangement with the IMF, agreed after June 2016.

Figure 4 shows a trend in the cumulative budget surplus/deficit measures for the entities, which shows that the last recorded surplus was in 2007. From 2008–14 there has been a steady budget deficit. In 2015, a minor surplus was recorded in the F BiH, mainly as a result of IMF pressures for fiscal tightening. The situation for 2016 is impossible to understand completely, as there are no official reports of the competent institutions on the state budget surplus/deficit for the last 12 months.<sup>2</sup> What we can see is an enormous debt servicing burden share in the budgets of the entities, particularly in the F BiH,<sup>3</sup> shown in Figures 4a and 4b,

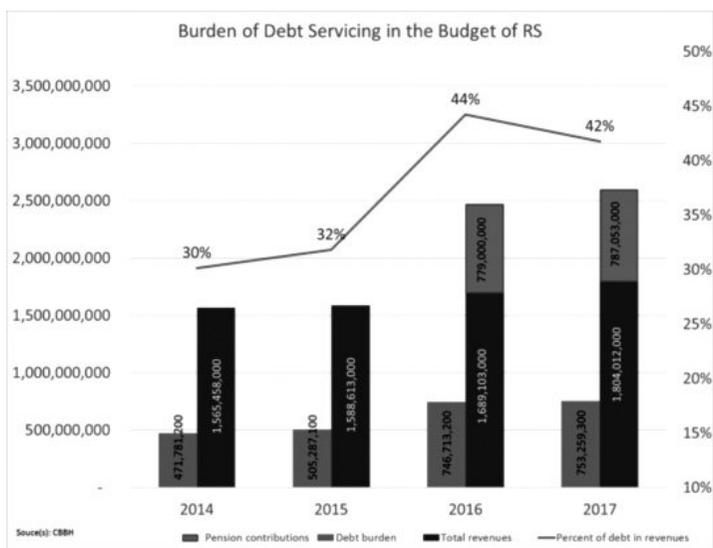
<sup>2</sup> However, analysis of the budget implementation for 2015 and the planned budget for 2016 is a visible continuation of the enormous debt for current consumption most often and in larger extent by issuing securities with short maturities, thereby destabilizing budgets, and makes the financial and monetary system unstable.

<sup>3</sup> However, a lower share of the burden of debt in the RS is actually relative because revenue from pension contributions in RS amounts close to 800 million, which is not the case in the F BiH because its off-budget fund.

**Figure 4a. Servicing of Government Debt and Budget Revenues in Federation of BiH**



**Figure 4b. Servicing of Government Debt and Budget Revenues in Republika Srpska**



instead of seeing a downward trend, one of the priorities of the Reform Agenda.

## **Section 2: Business Climate and Competitiveness**

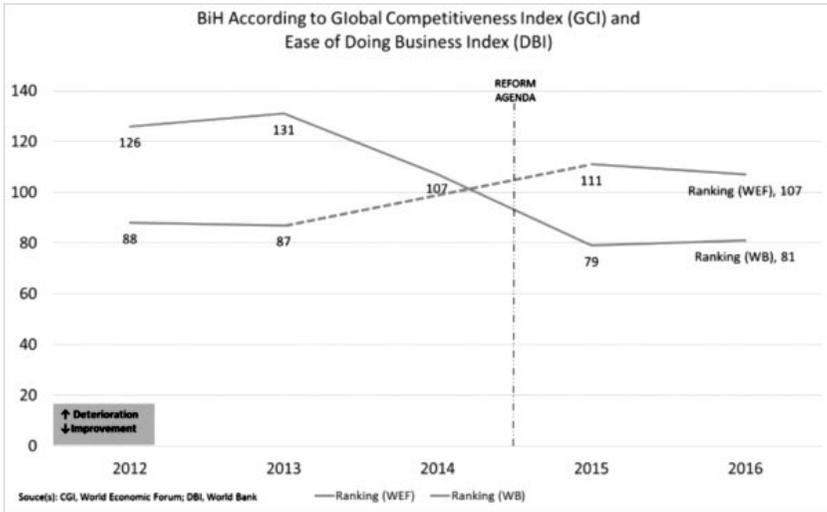
In the private sector, the Reform Agenda stands on the imperative that growth and prosperity must be based on attracting investments. There is a need to improve competitiveness by eliminating the well-known and documented obstacles to investments, such as political instability, corruption, red tape, cumbersome procedures, and complex tax systems. In addition, the inconsistencies and complexities of the regulatory framework and tax systems are often the main problems for potential investors, and are accompanied by high administrative barriers. Therefore, the Reform Agenda in this area tends to focus on simplifying procedures, strengthening motivation, and improving the overall environment for investments and start-ups.

Below are some indicators showing the trends in the last six years, including the year of the adoption of the Agenda.

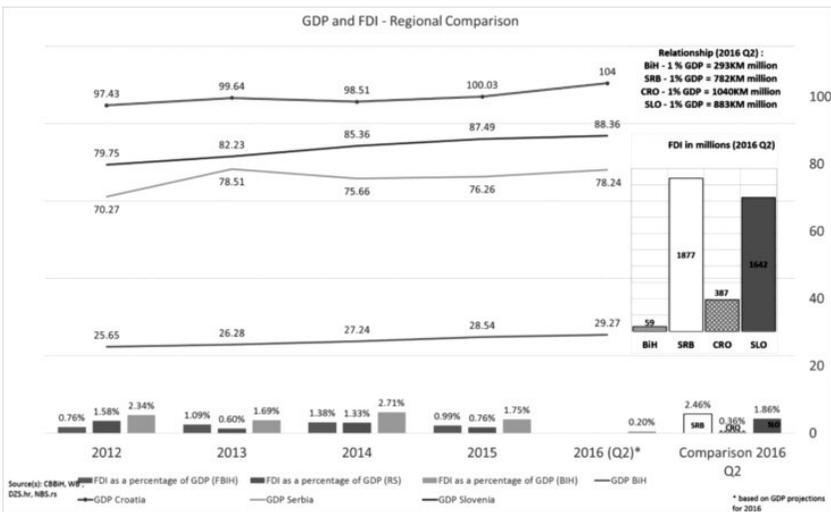
Figure 5 shows the comparative ranking of BiH in the Global Competitiveness Index (GCI), the World Economic Forum (WEF), the Index of Doing Business (DBI), and the World Bank (WB), in the period 2010–2015/2016. The scale bar represents 140 countries worldwide. The higher the position on the scale (closer to the value of 140), the worse the country's ranking, while a lower position indicating a better global ranking. The general impression is that the past six years saw no significant changes if we look at the ranking of the WEF methodology. On the other hand, the WB provides quite optimistic indicators for the last two years, although the best ranking (79th global position in 2016), is still considered a poor global position on average.

The level of foreign investment is proportionally affected by the business climate and ease of doing business in a country. Figure 6 depicts the Foreign Direct Investments (FDI) share of GDP of BiH during the period 2010–16, for the two entities and for BiH as a whole. It is evident that during the six years shown, the share of FDI oscillates between 1.69 percent and 2.72 percent of GDP, whereby in 2015 a serious decline is recorded. Compared to the region, (Serbia's FDI accounts for 5.3 percent of GDP, Slovenia for 2.1 percent of GDP), we demonstrate a very serious challenge that BiH must face in attracting FDI. Especially indicative is an insight

**Figure 5. Business Environment in Bosnia according to the WB and WEF**



**Figure 6. FDI share of GDP—comparative regional representation**



into the real value of GDP of the mentioned countries, where it is visible that Slovenia, whose population is smaller by three times, and Croatia almost four times higher GDP. In view of this their ability to attract FDI flows is much higher in absolute terms compared to BiH.

### **Section 3: Labor Market**

The Reform Agenda aims for the revitalization of the labor market, primarily by activating the underutilized labor force. The low activity rate of the working age population and the country's high unemployment rate, which is to a large extent the result of a mismatch of supply and demand for the qualified labor force, limits the possibilities for development. In BiH, there is a large number of long term unemployed and discouraged workers, and the unemployment rate is among the highest in Europe. New labor legislations and other policy reforms should provide an incentive for the labor market, increase the amount of work places, and decrease unemployment rates.

Figure 7 compares the active labor force to the total working age population. The share of the working-age population to the total labor force is worryingly low, only 45 percent, which means that as many as half of the working age population is not active in the official labor market. A large number of them is either under social welfare programs, in the gray economy, or socially excluded. Such a high inactive labor rate is the highest in Europe,<sup>4</sup> so this indicator is often used as a crucial instrument of showcasing the poor economic situation in the country, critically large gray economy, rigid labor market, and poor living standards.

Figure 8 indicates that the unemployment trend remained steady for several years without significant changes, indicating a worrying stagnation in the labor market with an extremely high unemployment rate and very low employment rate. However, in the last 18 months, the negative trend has stopped, and the unemployment rate was lowered by 2 percent. The public expects much better results in this area of the Reform Agenda, especially according to the opinion of "common citizens."<sup>5</sup>

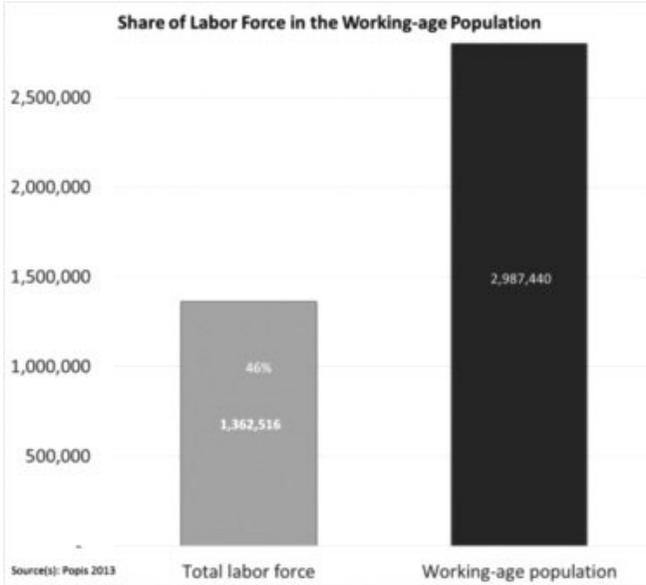
The salary difference between the public administration and the private sector is worryingly high in favor of the public administration (51 percent),

---

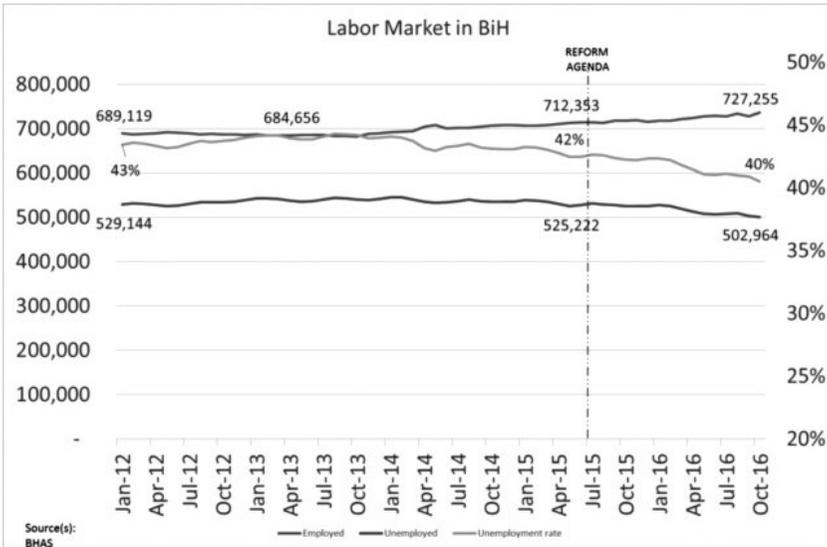
<sup>4</sup> World Bank, Organization's Open Knowledge Repository.

<sup>5</sup> USAID Project JSDP II, public opinion survey, [www.usaidjsdp.ba](http://www.usaidjsdp.ba).

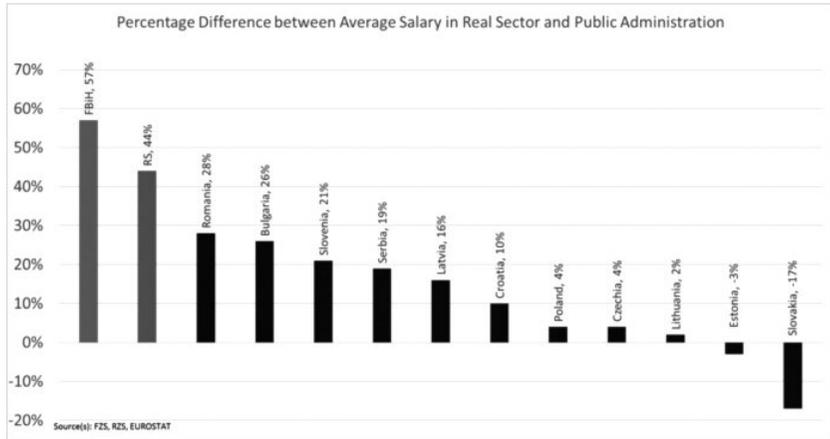
**Figure 7. Labor Force Activity**



**Figure 8. Number of Employed/Unemployed and the Rate of Unemployment**



**Figure 9. Difference in Wages between Public Administration and Real Sector**



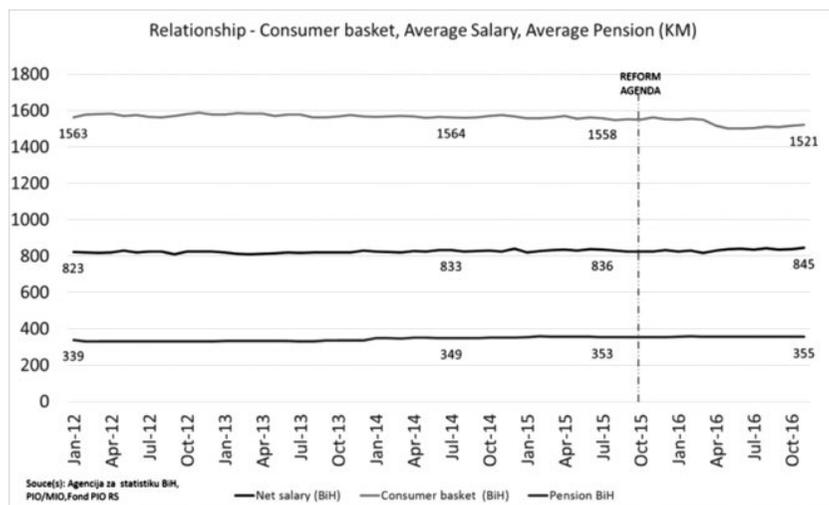
and as such, it is the highest in Europe. This area has recorded minimal changes in the last six years, and the sporadic movement of government savings had no significant impact on this relationship. The Reform Agenda is expected to contribute a significant change in this relationship.

### **Section 4: Social Security and Pension Reforms**

In this area, the Reform Agenda holds that a modern society should care for those who cannot look after themselves. However, the social welfare system should not interfere with incentives in the economy, and has to be fiscally sustainable. In order to achieve these objectives, the BiH government must improve social assistance targeting through a package of measures which will make the policy of social protection more efficient, effective and equitable. Pension systems should have a stable financial basis if the problem of a low living standard for pensioners is to be solved in the medium term.

Additional evidence for the stagnation in economic activity and a low living standard is provided in the relationship between the consumer basket, average salaries, and pensions (Figure 10). During a six-year period, net wages increased by about 4 percent in both entities, while the cost of the consumer basket grew until the beginning of 2015, when, due to deflation, it registered a decrease of about 4 percent. Average salaries and

**Figure 10. Relation between the Consumer Basket, Average Salaries and Pensions**

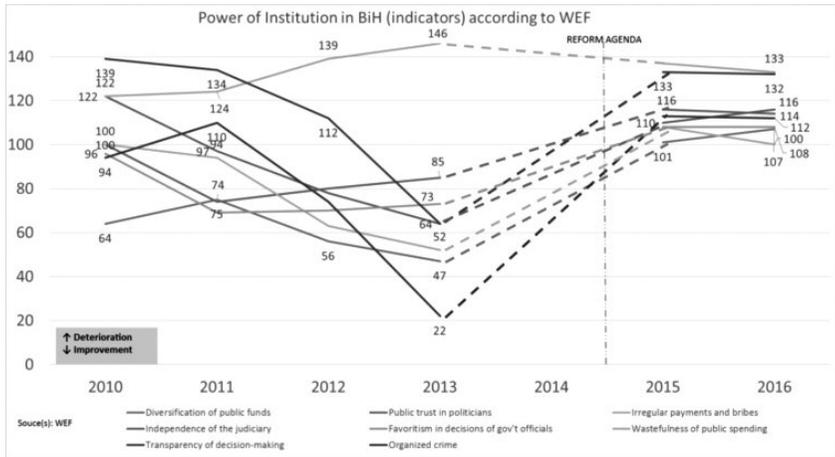


pensions remained stable throughout the period. Through these indicators we prove that there is economic stagnation and absence of the expected improvement in living standards, which would have been shown by an improved coverage of the consumer basket by average salaries and pensions.

The pension system in both entities is permanently destabilized and fiscally unsustainable. The best indicator for this claim is the ratio of the number of employees to the number of retirees. In the last five years, this ratio does not improve; on the contrary, the current ratio is completely unsustainable in the so-called system of intergenerational solidarity, which requires a minimum of three employees per retiree to remain sustainable for the economy.

Part of the problem with the pension system, is an accumulated deficit due to tax evasions. In fact, the tax debt of public institutions threatens the pension and health systems, produce a deficit, and result in the decline in quality and widespread corruption. The total debt due to unpaid taxes and social contributions exceeds 3 billion BAM. It is here that we can find part of the reason for the unregulated market, the negative public percep-

**Figure 11. The power of BiH Institutions**

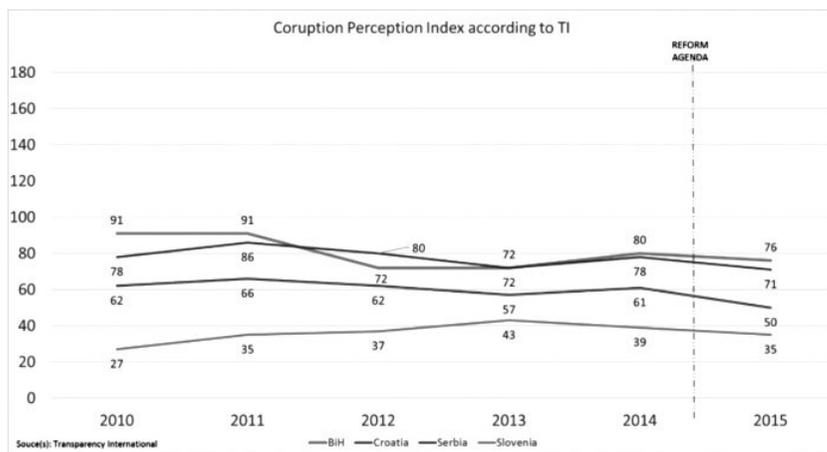


tion of public institutions and the legal system, and the most concrete source of the gray economy.

### Section 5: The Rule of Law and Good Governance

The Reform Agenda in this area aims to strengthen the rule of law, which must be built on the basis of concrete progress in the fight against organized crime and widespread corruption. All operational and institutional activities will aim to provide citizens with a safer environment without corruption. At the same time, the authorities are expected to provide confidence in the institutions responsible for the rule of law, capacity development, accountability, professionalism, and integrity.

Figure 11 presents a package of indicators by the WEF, where we can see a poor overall performance, with somewhat more positive trends in the last two years. We see very low performance in the indicator of wastefulness of public spending, transparency of decision-making, independence of the judiciary and public trust in politicians, which give an accurate picture of the essence of the problem. The ratings on these criteria clearly indicate a serious challenge that lies ahead in building the rule of law, fighting against corruption and political patronage, and establishing an independent judiciary system. An independent and efficient judiciary, and

**Figure 12. Corruption Perceptions Index—BiH and Countries in the Region**

professionalized, efficient and de-politicized institutions are the only guarantors for a strong rule of law.

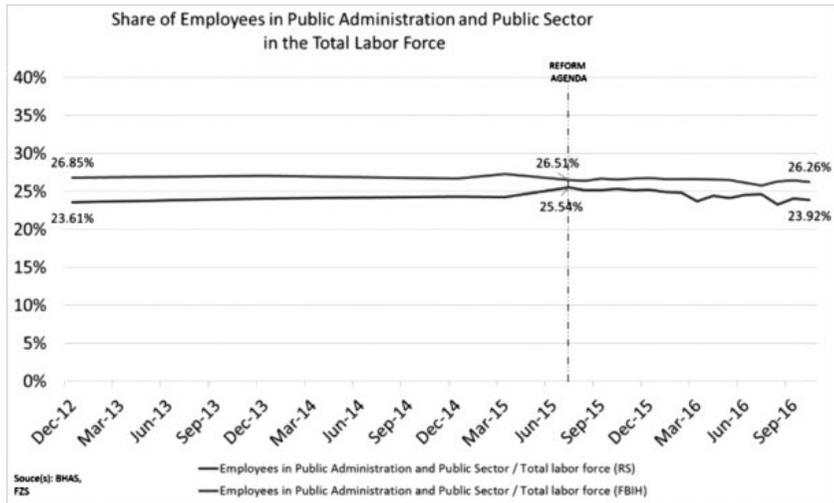
The fight against corruption is not yielding the expected results. Figure 12 provides a six-year trend of Corruption Perception Index (PCI) by Transparency International, with data for Bosnia and Herzegovina and three states in the region. The rank of BiH worsened by 4 positions in the last two years, and for two years in a row, Bosnia and Herzegovina, Albania, and Kosovo are the lowest ranked countries in the region, comparable to countries like Benin and El Salvador. Other sources<sup>6</sup> that measure the level of corruption in BiH through empirical and other methods, equally lead to the conclusion that corruption is perhaps the greatest social disorder in BiH, negatively impacting the business environment, the rule of law, trust in government institutions, the existence of a free market, and so on.

## Section 6: Public Administration Reforms

Public administration reforms are a key priority to ensure fiscal sustainability and quality service delivery to citizens.

<sup>6</sup> See GRECO EVAL IV Rep (2015), [www.apic.ba/izvjestaji](http://www.apic.ba/izvjestaji).

**Figure 13. Percentage of Employees in Public Administration and Public Sector**



More than a quarter of the budget is spent on salaries of public servants. Figure 13 shows the ratio of employees in the administration to the total number of employees during the course of six years. Contrary to the declarative paragraphs of government and political officials, the changes are minor and prove perennial continuity. The number civil servants in the two entities is higher compared to countries in the region, and is also above the average of EU and OECD countries. The entities’ share of public officials to those employed is at approximately 25 percent, while the average EU and OECD countries share is below 15 percent.<sup>7</sup>

### Beyond Reform Agenda—Back to the Future

Without structural, primarily constitutional and economic reforms, the future of Bosnia and Herzegovina is extremely questionable. Twenty years after the war, the present geopolitical and regional motives to destabilize the situation in Bosnia, the internal centrifugal forces and disintegration of society strongly determine almost all of the processes and phenomena

<sup>7</sup> OECD statistics, “Government at a Glance,” 2015 edition, indicator Employment in Public Sector as a Percentage of Total Employment.

in the country. Due to the absence of the rule of law, equality before the law, an independent and efficient judiciary, an autonomous and efficient public administration, a regulated market and institutional system capable of protecting the public order, any attempt to reform public policy is sentenced to blockades, obstructions, deformities, and ultimately to limited or no success at all.

The de-politicization of the public administration and zero tolerance for corruption are a *sine qua non* for initiating and implementing further reforms, which have come to be considered the property of the new generation of leaders in Bosnia and Herzegovina, because the change of generations is a necessary precondition for the withdrawal of past goals, and focus on the future.

The Reform Agenda has the capacity to reanimate long-delayed, transitional reforms, but in the course of the implementation of the Agenda, it turns out that political will is one precondition for success, and the structural reforms beyond the Agenda, the other.

It is important to implement crucial constitutional reforms in two directions: on the one hand, towards ensuring equal political and human rights for all citizens, regardless of their ethnic group or the territory in which they live; and on the other, optimizing the political and electoral systems. This can be done by easing the decision-making process, reducing veto points for blockages, strengthening and de-politicizing institutional powers, strengthening the instruments of political responsibility (rapid recall of legislative and executive powers) towards higher levels of cohabitation of individual and collective rights and instruments of protection, and contributions towards minimizing ethnic tensions and the protection of people living on territories where they represent a minority.

Furthermore, fundamental reforms must take place guided by the imperatives of de-politicization, increasing the efficiency and effectiveness of the public administration, including the strengthening of the independence of the judiciary, civil, and public services (education, health, etc.). The high level of corruption, especially at the highest levels of decision-making, through the so-called systemic—or political—corruption, is a consequence of clientelism and political patronage, which must be overcome by creating a merit-based employment and decision-making systems, management of public funds, public policy and public goods, and by establishing an efficient system of prevention and sanctioning of irresponsible and damaging public practice.

The Reform Agenda, therefore, instead of being a limited medium-term program, should be recomposed into a more permanent and strategic “Vision 2022,” which will go beyond the current mandate, and commit to a new set of elected representatives in the elections of 2018 towards the continuity and intensification of reforms. In the first place, structural reforms should last until 2020, at least in the normative sense, and until 2022 in order to produce tectonic reformist changes that will ensure internal integration, growth and development, but also secure membership of BiH to the EU, NATO, WTO, and other global associations.

In addition to the imperatives, objectives, and expected outcomes of the Reform Agenda, great care must be given to a fair, more balanced, and stimulating distribution of social wealth through the adjustment of the tax system, social welfare and veterans’ benefits, and a significant reduction of the gray economy and efficient and effective market regulation. The redefinition of rules that define and govern the education system and public health care system should be put high on the agenda and become the top priority, especially in terms of bringing an end to the conflict between public and private motives of the holders of public service in the whole public sector.

The issue of efficient market regulation is a prerequisite for improving the business environment without unfair state interventions in public and publicly-favored private companies, and the elimination of corruption in public procurement, issuance of business permits, inspection, and process complaints. A causal link between reducing the gray economy and better regulation of the market will be reflected in the stabilization of public finances, social, health and pension funds, establishing a favorable business environment, investment growth and jobs. Again, a prerequisite for the modernization and regulation of markets and the elimination of the gray economy is responsible public policy, zero tolerance towards erosion in the implementation phase, which includes a de-politicization and professionalization of government agencies responsible for the implementation of the new reform vision.

Two decades after the Dayton Peace Agreement, Bosnia and Herzegovina is at a crossroads of ideological, cultural, constituent, political, and economic choices, upon which it must build its future. Completing the transition from a socialist planned economy towards market capitalism, from a one-party centralized policy towards a pluralistic constitutional parliamentarianism, from a de-nationalized authoritarian regime into a multiethnic community, from the culture of collectivism and totalitarian

dogma to a society of free speech, individual expression and association, and from a society with growing social stratification, segregation, and discrimination, into a society of equal opportunities, social justice and ethical motivations.

## *Chapter 9*

# **Challenges and Expectations for Reform Activities in BiH: The Perspective of Republika Srpska**

*Darko Milunović and Boris Tučić*

Beginning a process of economic revival and modernization that would foster viable, efficient, stable, and socially just economic growth are only a few of the priorities for the reform path of BiH. Creating new employment opportunities, better and more effective distribution of social benefits and creation of just business environment should be the epilogue of all these reform processes. If the path taken by Republika Srpska, FBiH, and BiH is to be successful, it is necessary to continue activities that would improve the rule of law, combat corruption, and enhance the efficiency of public institutions through what has been stated as an unequivocal determination by all actors.

The reform path of BiH is formally defined by the Reform Agenda (RA), which should be realized by 2018 and which includes a wide set of medium-term priorities that serve as the basis for setting very concrete objectives and development guidelines. The Agenda, which has been agreed on with international financial institutions and the European Union, represents the starting point for talks about individual programs of financial and technical assistance, and that by itself proves its relevance. The RA and the Program of Economic Reforms of Republika Srpska for the period 2017–19 are also the framework for the writing of this chapter.

The chapter consists of an introduction, three separate but closely connected parts, and a conclusion. The first part provides a short description of Republika Srpska, one of the two entities of Bosnia and Herzegovina, and provides a list of its advantages for potential investors and also provides an answer to a question: Why invest in Republika Srpska? The second part provides a detailed description of the macroeconomic situation in Republika Srpska and in Bosnia and Herzegovina as a whole, taking into account global developments and regional tendencies, whereas the third and key part refers to ongoing reforms and their expected results.

## Republika Srpska, an Entity Within BiH

Republika Srpska, one of two entities within BiH, due to its geo-strategic position in the heart of South East Europe and on the very border with the European Union, is an ideal place for investment. Geographically and traffic wise, RS has a peculiar position and relevance being intersected by vital communications connecting the Balkans, Europe, and Asia.

The city of Banja Luka, as the biggest business and administrative center of RS, is connected to the most important transport passageway in the region, Paneuropean Corridor X, and with the International Airport Banja Luka, which at the moment performs both passenger and cargo traffic, should become one of the most important pillars of the development of Republika Srpska. Banja Luka has been recognized as a regional center and declared a reformer in the improvement of the business environment in South-East Europe by the World Bank Doing Business Report from 2011.

Inhabitants of Republika Srpska are traditional and very proud. Daily life is deeply rooted in a rich tradition, cultural heritage, and the abundant natural resources in RS. Republika Srpska has abundant natural resources and an ideal combination of the moderate continental, mountain, and mediterranean climate. Natural wealth gives Republika Srpska a conspicuous advantage in food processing and wood industries. Due to hydro power and coal reserves, RS is among the most significant producers and exporters of the electricity. Natural goods also provide the grounds for tourism development. Jahorina, an Olympic Mountain from the 1984 Sarajevo Olympics, is the jewel among them, where lately we saw increases in health tourism (spa tourism and dental services) due to a qualified medical staff. Nevertheless, the largest exporters in Republika Srpska come from the metal industry, primarily due to a competitive labor cost, good geographic position, low transportation costs and significant raw material resources.

The RS population is 1.3 million, but its market openness and free trade agreements (FTAs) enable the businesses in Republika Srpska to access a market of close to 600 million people.

On the one hand, as the result of signing the Stabilization and Association Agreement, Republika Srpska can export all goods that meet EU quality standards to the European Union. On the other hand, the countries of the region have improved their economic and trade exchange by signing

the CEFTA Agreement at the end of 2006 (entered into force on May 1, 2007), which gave access to a market of 30 million people. Due to some other agreements signed, Republika Srpska has access to an even larger market, and that makes it very attractive for foreign investors.

Tax free trade and an encouraging tax policy provide for lower costs for business activities and starting a new business in RS. The tax policy in Republika Srpska is one of the most encouraging in the region, and there is an intention to improve it even further. As a matter of fact, the new Law on Corporate Income Tax, the income from dividend and profit share are exempt from income tax payment and this mere fact makes RS even more attractive for investments. The value added tax (VAT) is 17 percent, which makes it one of the lowest in Europe (it is lower only in Luxembourg). The profit tax of 10 percent is the lowest in Europe.

As for the engagement of labor, investors can count on full support of the RS Employment Institute, which can recruit qualified and experienced workers within a short period of time. It is important to mention that the ratio between the quality of the labor and the average salary is very good. The average net salary in Republika Srpska is 420 euro, and the cumulative contributions rate is 33 percent, with the intention to decrease it even more. The Personal Income Tax is also the lowest in Europe and amounts 10 percent, while the nontaxable income is 100 euros.

Additionally, electricity prices are the lowest in the region, there is a low cost for all communal services, and good prices for the rent or purchase of business premises. Moreover, business registration takes approximately three days to complete. Keeping all this in mind, it becomes clear that RS has excellent preconditions for doing business.

Finally, foreign and domestic investors in Republika Srpska are subject to the same regulations. In other words, any investor can own a real property in Republika Srpska, open an account in any commercial bank, employ foreigners, and transfer their profit abroad. One additional benefit for foreign investors is that foreign capital invested through equipment is exempt from import customs and customs fees.

In order to create an encouraging business environment, the RS government and local governments make a continuous efforts to eliminate bureaucratic red tape. At the same time, all relevant RS institutions and representative offices abroad are available to foreign investors.

## Macroeconomic Framework in BiH and in Republika Srpska

To understand the macroeconomic situation in BiH and in Republika Srpska, we must also look at global trends. This chapter offers the main characteristics of the global economy and the EU economy.

According to the latest IMF Report,<sup>1</sup> the World Economic Outlook (WEO), which analyzes global economy developments, the global growth projection for 2016 is 3.1 percent, and 3.4 percent for 2017. The projections for the second half of 2016 and 2017 were revised to reflect weakened growth prospects for the developed economies after the referendum in the U.K.,<sup>2</sup> and a weaker than expected growth in the US. Consequently, modest growth in developed economies has been projected to stand at 1.6 percent in 2016 and 1.8 percent in 2017. As for the Eurozone, a growth of 1.7 percent in 2016 and 1.5 percent in 2017 has been forecast as the result of low oil prices and economic incentives offered by the European

**Table 1. Real GDP Growth (IMF projections)**

	2014	2015	2016	2017
Real GDP Growth, %				
World	3.4	3.2	3.1	3.4
Developed economies	1.9	2.1	1.6	1.8
USA	2.4	2.6	1.6	2.2
Euro Zone	1.1	2.0	1.7	1.5
Developing countries	4.6	4.0	4.2	4.6
European Union	1.6	2.3	1.9	1.7
European developing countries	2.8	3.6	3.3	3.1
BiH	1.1	3.2	3.0	3.2
World trade growth (goods and services), %	3.8	2.6	2.3	3.8
Oil prices growth, in US dollars, annual change, %	-7.5	-47.2	-15.4	17.9
Consumer prices				
Developed countries	1.4	0.3	0.8	1.7
Developing countries	4.7	4.7	4.5	4.4
BiH	-0.9	-1.0	-0.7	0.5

Source: IMF, World Economic Outlook, Update October 2016.

<sup>1</sup> October 2016.

<sup>2</sup> Even though the market reaction to Brexit was encouraging, the final effect is still unclear due to the uncertain fate of institutional and trade arrangements between the U.K and the EU.

Investment Bank. The projection for European developing countries is 3.3 percent growth in 2016 and 3.1 percent in 2017, whereas the projected rate of real GDP growth for BiH in the 2016–2019 period is 3 percent, 3.2 percent, 3.7 percent and 3.9 percent, respectively.

Foreign direct investment (FDI) inflow recorded a significant recovery in 2015. Worldwide, there was a 38 percent rise of FDI, the biggest since the global economic and financial crisis. It is expected that FDI would drop between 10–15 percent in 2016 as the result of the global economy's vulnerability, weak demand, low export of goods in certain countries, tax evasion, and the fall of profits for multinational companies. Nevertheless, in the medium term it is expected that FDI in 2017 and 2018 would rise as the result of global economic growth.

In Republika Srpska, according to the data of the RS Institute for Statistics, the real GDP growth rate in 2015 was 2.6 percent. After the floods in 2014, there was a fall in the second quarter and stagnation in the third quarter of the year, leading to larger growth in 2015. Besides, the GDP growth in 2015 was mostly due to an increase in private consumption.

As for other macroeconomic indicators described in more details further in the text, it is clear that developments with relation to previous years are mostly positive, a positive sign for reforms.

The average net salary in RS is relatively stable, and amounted to 831 BAM in 2015 (more than 420 euros), which is a nominal rise of 0.7 percent when compared to 2014, but in reality, it represents a 2.2 percent rise once deflation is taken into account. The average net salary in 2016 is expected to remain at approximately the same level.

The labor market is gradually recovering. This is supported by an unemployment rate of 25.2 percent in 2015, equaling a fall of 0.5 percent from the previous year. This trend continued in 2016 when the unemployment went down to 24.8 percent. Accordingly, the number of unemployed in 2015 (139,465 persons) shrank by 4.4 percent, whereas the figures for 2016 are even better (the number of the unemployed in September 2016, according to the official records is below 130,000). Positively, the number of employed is going up at the same time, and in September 2016 it totaled 257,001 persons, which is a 3.3 percent increase from the same period last year. By analyzing the statistical figures of the labor market, we see that the unemployment rate is falling, while the employment rate is rising.

The foreign trade exchange in 2015 was seven billion BAM, which shows a fall of 8.6 percent compared to the previous year. A larger fall of import (11.7 percent) in relation to exports (2.9 percent) resulted in a decrease in the trade deficit so that the export-import coverage was 5.4 percent higher than in 2014. In this notion, the data for the current year also demonstrates an improvement compared to the previous year. In concrete terms, trade in the period of January–September 2016 is characterized by a lowering of the trade deficit by 18.2 percent, as the result of increased exports (by 8.7 percent) and decreased imports (by 2.3 percent), whereas the export-import coverage is 65.5 percent. In terms of time, export-import coverage has improved year after year, which is viewed as a positive indicator. In the last 10 years, from 2006–2016, the export rate grew twice as much as the import rate (geometrical growth rate).

Speaking of macroeconomic assessments and projections for RS in the 2017–2019 period, a stable economic growth is expected at the rates of 3 percent, 3.2 percent, and 3.3 percent, respectively. This is mostly as the result of industrial production growth, expected rise of economic activities in the area (especially with the largest foreign trade partners) which can maintain a certain level of export demand, mild growth of domestic demand due to higher employment and the positive effects of investments. In the three-year period, it is expected that average consumer prices will rise by 0.1 percent in 2017, 1.1 percent in 2018, and 1.4 percent in 2019. It is also expected that average net salaries will record a mild growth: 843 BAM in 2017, 850 BAM in 2018, and 859 BAM in 2019. Unemployment rates are projected to drop to 24.4 percent, 24 percent, and 23.6 percent, respectively.

At the end of this part, it is important to look at indebtedness as a relevant factor of the overall economy. Even though at the moment the debt level is close to the limit of 60 percent of GDP,<sup>3</sup> the forecast projects that this limit will not be overstepped in the near future. According to the projections of the RS Ministry of Finance, which are included in the Program of Economic Reforms for the 2017–2019 period, all debt indicators show a declining trend. In 2017, the overall debt (i.e., public debt in relation to GDP) would be 59.5 percent. By 2018, it will be 58.8 percent and 44.8 percent, and in 2019, it will be 56.6 percent and 42.7 percent respectively.

---

<sup>3</sup> One of the so-called Euro convergence criteria, defined in Maastricht in 1992, on the basis of which the readiness of the EU member state for the third phase of economic and monetary union is evaluated.

**Table 2—Breakdown of macroeconomic indicators for 2012–15 period, assessment for 2016 and projections for 2017–19**

Description	2012	2013	2014	2015	2016	2017	2018	2019
GDP								
GDP nominal, in mil. BAM	8,585	8,761	8,847	9,153	9,501	9,890	10,325	10,790
No. of inhabitants – in millions	1.43	1.43	1.42	1.42	1.41	1.41	1.41	1.40
GDP per capita in BAM	6,006	6,146	6,225	6,465	6,725	7,015	7,340	7,686
% of GDP growth, nominal	-1.1%	2.1%	1.0%	3.5%	3.8%	4.1%	4.4%	4.5%
% of GDP growth, real	-1.1%	1.9%	0.2%	2.6%	2.9%	3.0%	3.2%	3.3%
Inflation measured by the consumer price index (CPI), average annual rate	2.1%	0.0%	-1.2%	-1.4%	-1.2%	0.1%	1.1%	1.4%
Real GDP growth	-1.1	1.9	0.2	2.6	2.9	3.0	3.2	3.3
Private consumption*	2.9	1.8	2.1	1.9	1.9	2.1	2.2	2.2
State consumption	2.6	0.8	2.0	-1.8	1.1	0.8	0.9	0.7
Gross investments in means of production	11.0	-5.0	5.4	-0.2	3.1	3.2	3.4	3.8
					(nominal growth rate %)			
Assumptions:								
Average net salary in BAM	818	808	825	831	836	843	850	859
Import of goods in mil. BAM	4,488	4,558	4,946	4,369	4,346	4,503	4,719	4,955
Import of goods, annual growth in %	-2.0%	1.6%	8.5%	-11.7%	-0.5%	3.6%	4.8%	5.0%
Export of goods in mil. BAM	2,375	2,604	2,692	2,614	2,792	2,956	3,169	3,404
Export of Goods, annual growth in %	-7.3%	9.7%	3.4%	-2.9%	6.8%	5.9%	7.2%	7.4%
Export-Import coverage %	52.9%	57.1%	54.4%	59.8%	64.2%	65.7%	67.2%	68.7%
Unemployment rate %	25.6%	27.0%	25.7%	25.2%	24.8%	24.4%	24.0%	23.6%

Source: Institute of Statistics of Republika Srpska (2012–2015), assessment (2016) and projection (2017–2019) of the Ministry of Finance of Republika Srpska.

## **Directions of the Reforms in Republika Srpska in the Upcoming Period**

The main program goal of RS institutions has always been a strong, democratic, and prosperous entity vested in all its competences verified by the Dayton Peace Accords, open to the world and capacitated with institutions that can respond to the needs of its citizens.

Based on a clear program goal, taking into consideration macroeconomic situation and trends, starting from the policies set by the Reform Agenda for the 2016–2018 period and corresponding Action Plan agreed with the European Union and international financial institutions, key reform areas for Republika Srpska are: public finance, primarily the reduction of the tax burden on labor, health care, business environment, an enhanced labor market through improved ties with education reforms, continuation of infrastructural projects especially in the areas of energy and communal infrastructure, sector development based on the reform of public enterprises, improvement of the agriculture and finance sectors.

Taking all these directions into account, the Program of Economic Reforms of Republika Srpska for the designated period includes the following guidelines:

- Public Finance Management;
- Energy, Transport, and Telecommunications Markets;
- Sector development;
- Business Environment and Shrinking of the Informal Economy;
- Research and Innovation;
- Foreign Trade and Facilitation of Investments;
- Education and Skills;
- Employment and Labor Market and;
- Social Inclusion, Reduction of Poverty, and Equal Opportunities.

The positive side of this new package of reforms (the Reform Agenda), is that activities are coordinated and carried out simultaneously at all levels of government, which is extremely important for a decentralized country such as BiH. This is also a confirmation that the decentralized structure of the country is no obstacle to reforms and development, if activities are coordinated. To date, reforms and similar measures have been implemented more or less separately without particular coordination between various

levels of governance, very often having different regulations in the two entities which, constitutionally, are the main bearers of development in BiH.

For example, Republika Srpska is in charge of the economy, agriculture, energy, infrastructure, ecology, health care and social protection, education, labor, employment and pension system, and local development, all areas that matter to the everyday life of its people.

The results achieved in Republika Srpska, the Federation of BiH, and at the level of BiH institutions are fairly promising and are indicative of a successful outcome. More precisely, all levels of government adopted their action plans for the implementation of the RA and ensured regular monitoring of its implementation in cooperation with the EU. The results are encouraging since all activities planned for 2015 and 2016 have either been fully implemented or are ongoing.<sup>4</sup> A similar situation is true in the FBiH and at the BiH level.

Even though the reforms represent a comprehensive set of measures, we have identified several additional key areas in need of reform. Aside from the private sector, large enterprises owned by RS are also important employers and significant contributors to economic development. Unfortunately, those enterprises stick to their outdated business habits and have not developed as much as expected, thus it is fitting that an important part of the measures target those enterprises (belonging to the sectors of forestry, energy, railway traffic, road infrastructure, postal traffic, and others). Some of the reforms in this area are implemented along with international financial organizations, for example the World Bank, which is involved in the reorganization of the RS Railways. Other public enterprises have been classified as viable and non-viable, the possibilities for their restructuring or privatization have been identified and activities on the revival or sale of some others have started.

The process of privatization has advanced more in Republika Srpska compared to the Federation of BiH. The privatization process was designed within the framework of the reforms initiated by and implemented in cooperation with the international community, demonstrating weakness across Europe, including the countries of Central and Eastern Europe.

---

<sup>4</sup> In the RS, 51.4 percent of activities have been finalized and 47.3 percent are ongoing, while only 1.4 percent are not realized. The implementation of certain measures foreseen for 2017–2018 have already begun, demonstrating a serious approach of the government to the reform process.

It is also important to mention that Republika Srpska founded the Investment-Development Bank by the collected funds gathered through the sale of RS Telecom and the oil industry. As a matter of fact, 49 percent of the funds collected in this way have been used for important infrastructure projects and other projects in RS municipalities, while 51 percent of the capital remained permanently in the ownership of Republika Srpska.

Health care is one of the areas included in the Reform Agenda. In Republika Srpska, health care falls under the entity's administration, while in the Federation of BiH it belongs to the cantons. With the World Bank, efforts are underway to identify debts in this area and introduce greater discipline and recovery measures. One of the measures is the introduction of a treasury system in hospitals and health centers, a project which is implemented in cooperation with USAID.

Many reforms in the financial sector are currently underway. A set of new laws related to the banking sector are being defined in cooperation with the IMF in order to strengthen the position of banks, their oversight, and supervision of their work. The intention is to have a harmonized banking regulation in both entities. Improving data exchange between tax administration authorities within BiH is also under way, and Republika Srpska passed a set of laws targeting the gray economy.

An important focus of the reforms pertains to the rationalization of public administration, or the public sector. A moratorium on salary increment and admission of new workers has been imposed in order to prevent the uncontrolled growth of the administration. Work on preparation of the Public Finance Management Strategy of Republika Srpska for the 2016-2020 period is completed, and the modernization of tax laws is pending.

One of measures implemented to unburden the economy was the creation of a Register of Parafiscal Charges. In cooperation with the IMF Mission, many activities related to reduction of the tax burden on labor have been launched, while at the same time finding real and stable sources of financing that would compensate for the lower influx of tax revenue.

Within the Reform Agenda, concrete steps are taken to improve the business climate and to increase competitiveness. Prior to the Reform Package, the RS government implemented certain projects relevant to the improvement of the business environment. Several years ago, the government carried out the business registration reform and applied the One-Stop-Shop model, which enormously reduced the costs and time needed for registration of private sector entities. This reform is now being carried

out in the Federation of BiH. Within the Reform Agenda, a second phase of the Project would be to implement online business registration. The procedures for obtaining construction permits have been accelerated, and some other reforms in this area are planned.

With regard to labor market reform, a new Law on Labor was passed a year ago, which provides solutions that offer higher flexibility of work conditions and differentiated salaries based on skills, qualifications, professional experience, and performance.

An important reform was carried out in RS by passing a new Law on Bankruptcy. The Federation of BiH is currently working on an identical law that would contribute to increased efficiency of the whole process and harmonization of regulations in both entities.

Both entities have yet to face serious reforms in the sectors of secondary and higher education, with the final aim to foster better connectivity between the education system and the needs of the labor market. Education falls under the competence of the RS entity, but in the FBiH it is the responsibility of the cantons.

Rule of law, good governance and increased security are constant challenges for all governments. Republika Srpska is developing capacities for the fight against terrorism and adopted the Action Plan for the fight against terrorism for the 2016–2020 period. One of the priorities is fighting cyber-crime, where excellent cooperation with services from the US has been established. The new Law on Combating Corruption, Organized Crime and Severe Economic Crime has also been passed in Republika Srpska. Furthermore, an Operational Agreement with EUROPOL has been concluded which facilitates efficient data exchange.

In the first part of this chapter we referred to the business environment and investment opportunities in Republika Srpska, but we also have to mention certain facts which are important for domestic as well as for foreign investors:

- Encouraging tax policy—among the most encouraging in the region and in Europe;
- Quality labor and;
- Low electricity prices.

Besides, the rights of local and foreign investors are equal and guaranteed by the Constitution, including certain benefits such as exemption

from customs payment for the import of equipment as an equity share of the foreign entity, free transfer of profit, etc.

All of the facts referred above have been recognized as an investment potential, and have been supported by recent investments. One of those is large British-Chinese investment of over 550 million euro, and refers to construction of a thermal power plant. Another is an Italian investment of over 40 million euro for the construction of a silicon metal factory, as well as major infrastructure projects such as the construction of highways with the assistance of the European Investment Bank (EIB) and European Bank for Reconstruction and Development (EBRD). In addition, talks with Chinese companies on some major infrastructure and energy projects have started.

All the above stated is indicative that the most comprehensive and the furthest reform process in BiH and Republika Srpska are taking place, and that their final goal is to create a stable and modern economy following the example of advanced economies of EU members states. Support from international partners such as the European Union, IMF and the World Bank in a financial and technical sense is enormously important so that the demanding reforms could successfully be implemented. Therefore, one of key requirements before domestic and international partners, which has not been the case with some earlier initiatives, was a complete exclusion of the reform processes from the political sphere and placing the focus on joint coordinated actions that would lead to economic development and a better standard of living for citizens of Republika Srpska and the Federation of BiH.

## **Conclusion**

Reform activities in BiH (on the state-level, and on the entity level in the FBiH and RS), are based on a joint synergy of local institutional factors and international partners—including the European Union, the International Monetary Fund and the World Bank Group—and are proceeding in accordance to the anticipated dynamics. Taking into consideration the impetus, the depth, nature, and medium-term timeline of the reform processes, real effects are yet to be seen, even though the European Commission and international financial institutions reported positive results in 2016. The continuation of structural reforms in BiH and Republika Srpska are a guarantee for the facilitation of economic stability and are a precondition for strenghtening competitiveness of the local economy in

a European and regional framework, including an even greater influx of foreign investment in various sectors. At the same time, the successful continuation of reforms would enable Republika Sprska and the Federation of BiH to respond to European and global macroeconomic developments.

An important aspect to consider when analyzing the anticipated results of the Reform Agenda is the very moment of its implementation, i.e., the fact that the most comprehensive economic reforms (the Reform Agenda and the Program of Economic Reforms) come twenty years after the end of the armed conflict in BiH. This does not mean that the country has not been the subject of reform initiatives in the past, it means that previous measures were wrongly designed. Unlike the existing reform platform, which has been the result of a negotiating process between local actors and international partners, previous reform initiatives were often imposed by the international community, neglecting or underestimating the relevance and the role of domestic stakeholders in the process. Moreover, the majority of the reform proposals targeted the re-composition of the internal constitutional structure of BiH, without a consensus among key domestic political factors. While it comes as no surprise that previous reform attempts harvested dissapointing results, the existing platform of reforms is more promising, with a focus on the economy rather than on political and constitutional matters, and based on a general consensus of all relevant domestic actors.

The Reform Agenda recognizes the necessity to move away from BiH's label as a playground for various unsuccessful political initiatives and where all economic development has been completely neglected. In other words, instead of imposing big issue reforms which lack consensus of all key actors in BiH and consequently lead to dissapointing results, the international community should demonstrate their good intentions and partnership with BiH through their support of the implementation of economic reforms within the existing legal framework of BiH. Regardless of its complex internal structure, BiH can accomplish succesful reforms through coordinated activities and a harmonization of its valid laws and practices, and certainly not through the re-composition and unconstitutional centralization of powers at the level of BiH institutions.



## Chapter 10

# Reform Process in BiH: For Youth and With(out) Youth?

*Ajka Baručić*

At the state level of Bosnia and Herzegovina (BiH) there is no single law regulating youth issues. Since the administrative structure of Bosnia and Herzegovina consists of two entities—the Federation of Bosnia and Herzegovina (FBiH), Republika Srpska (RS), and the Brčko District, there are legislative and other strategic documents regulating and defining various issues, including issues concerning the life, position and activities of youth. Pursuant to the Youth Law of the Federation of Bosnia and Herzegovina<sup>1</sup> and the Law on Youth Organizing of Republika Srpska,<sup>2</sup> youth are defined as persons between the ages of 15 and 30. The Brčko District currently has no legislation regulating youth issues.

There are 773,850 young people in Bosnia and Herzegovina, which accounts for 21.91 percent of the country's total population, according to the data from the Census of population and housing in Bosnia and Herzegovina from 2013.<sup>3</sup> From that number, 51.3 percent of youth are male and 48.7 percent are female. The Census currently does not offer data for the educational structure, employment status, and other aspects for the youth population, as this data has not been disaggregated from the data of the general population. Given the fact that the last census in BiH was conducted in 1991, and that youth were defined as a discrete category of population only in 2004, pursuant to the Law on Youth Organizing of Republika Srpska,<sup>4</sup> and taking into consideration that all data concerning the number of young people in the period from 1991 to 2013 are merely

---

<sup>1</sup> Youth Law of the Federation of Bosnia and Herzegovina, "Official Gazette FBiH", No. 36/10.

<sup>2</sup> Law on Youth Organizing of Republika Srpska, "Official Gazette of Republika Srpska", No. 98/04, 119/08 and 1/112.

<sup>3</sup> Agency for Statistics of Bosnia and Herzegovina, *Popis stanovni\_tva, doma\_instava i stanova u Bosni i Hercegovini, 2013*, Juni 2016, <http://www.popis2013.ba/popis2013/doc/Popis2013-prvoIzdavanje.pdf>

<sup>4</sup> Amendments were made in 2012 according to the Youth Law of the Federation of Bosnia and Herzegovina.

estimates, it is difficult to monitor specific trends. That is precisely why the currently available official youth statistics are so immensely important, because however limited they may be at the moment, they provide the groundwork for further strategic planning and making decisions impacting the position of youth.

Given the lack and limitations of official statistical data, several studies, analyses and surveys on youth, authored mostly by non-governmental organizations help us understand youth in Bosnia and Herzegovina—what their problems and needs are, their attitudes, desires and expectations. The three most comprehensive surveys on youth in BiH are “Youth Need a Youth Policy—Analysis of the Position of Youth and the Youth Sector in Bosnia and Herzegovina,” written in 2008 by the Commission for Coordination of Youth Issues in BiH and the German Society for International Cooperation (GIZ), and the analysis “Voices of Youth” created in 2012 by the United Nations Development Program (UNDP), and the “Analysis of the Position and Needs of Youth in the Federation of Bosnia and Herzegovina in 2013,” developed by the Institute for Youth Development KULT in cooperation with the Federal Ministry of Culture and Sports. The results of all three analyses reveal alarming data on the position of youth for the period between 2008 and 2012.

The study presented in the document “Youth Need a Youth Policy—Analysis of the Position of Youth and the Youth Sector in Bosnia and Herzegovina”<sup>5</sup> shows that in 2008, almost one in two young people leaving formal education remain at the level of a three-year secondary education, or less, and one in four leave education early, which is significantly higher than the average in most European countries. All of this results in youth poverty and social exclusion. Furthermore, one in four employed young people hold jobs that are completely different from what they were educated to do, which causes a significant deficit in the knowledge and skills needed to perform a particular job. One quarter of youth in the 16–24 age group live in households with an average income lower than 430 BAM<sup>6</sup> i.e., 60 percent of the average income for the entire population (713 BAM). Only 7 percent of youth who live in low-income households receive some kind of welfare benefits. Data presented in the analysis “Voices of Youth”<sup>7</sup>

<sup>5</sup> Commission for Coordination of Youth Issues in BiH and German Society for International Cooperation GIZ, *Mladi trebaju omladinsku politiku—Analiza položaja mladih i omladinskog sektora u Bosni i Hercegovini*, 2008, [http://www.mladi.gov.ba/pdf/Analiza\\_mladi\\_-\\_za\\_web.pdf](http://www.mladi.gov.ba/pdf/Analiza_mladi_-_za_web.pdf)

<sup>6</sup> The exchange rate in May 2017 is 1 US dollar = 1.79 BAM.

<sup>7</sup> United Nations Development Programme, *Voices of Youth*, February 2012, [http://www.undp.org/content/dam/unct/bih/PDFs/VoY%20BHS\\_web.pdf](http://www.undp.org/content/dam/unct/bih/PDFs/VoY%20BHS_web.pdf).

shows that 3 out of 4 youth are unemployed, most are not married, do not have children or their own housing. Youth are pessimistic about the future, and rate their living standard as mediocre. They do not possess the skills needed to respond to the demands of a labor market exposed to modern technological trends. All these negative indicators are even more detrimental to vulnerable categories of youth.

The “Analysis of the Position and Needs of Youth in the Federation of Bosnia and Herzegovina for 2013”<sup>8</sup> shows that one third of youth leave education early, mostly due to financial reasons, while 88 percent of youth are not receiving any type of financial assistance. scholarship. When it comes to healthcare, only 40 percent of youth underwent a physical exam in the last 12 months, and half of this percentage of youth had a physical as part of a particular formal procedure, not as a regular check-up. Roughly 7 percent of respondents do not have health insurance, or are not aware that they are entitled to health insurance., and 23 percent of youth do not engage in recreational activities. In addition, 60 percent of youth cannot contribute to the household budget, and 23 percent live in households with an income lower than 1,000 BAM. Moreover, 29 percent of youth have no monthly income, 27 percent did not want to reply, and 16 percent have monthly incomes of up to 200 BAM. Only 5 percent have more than 1,000 BAM a month. 9 percent are married and 7 percent have children. 7 percent of youth have independent housing, 2 percent of which are tenants, while the remaining 5 percent are homeowners. One in two young people would like to launch their own business but need support; not only financial but also advisory and educational support. Although a substantial number of young people do not believe that their position will improve, there are still youth who managed to remain optimistic. A quarter of youth believe that their situation will improve somewhat, and 22 percent believe that there will be substantial improvement.

### **The Largest Problem of Youth in Bosnia and Herzegovina: Unemployment**

Unfortunately, unemployment is the first thought that comes to mind when one mentions the youth in Bosnia and Herzegovina. Unemployment is a problem faced by the general population as well, but is particularly

---

<sup>8</sup> Institute for Youth Development KULT, *Survey on the Position and Needs of Youth in the Federation of BiH 2013*, 2014, [http://mladi.org/index.php?option=com\\_phocadownload&view=category&download=455%3Asurvey&id=69%3Apublic\\_inst&Itemid=562&lang=ba](http://mladi.org/index.php?option=com_phocadownload&view=category&download=455%3Asurvey&id=69%3Apublic_inst&Itemid=562&lang=ba).

severe for the youth population. According to the Labor Force Survey<sup>9</sup>, the 2015 unemployment rate was 27.7 percent, while in 2014 and 2013 the rate was 27.5 percent. In 2015, the employment rate was 31.9 percent, in 2014 it was 31.7 percent, and in 2013 the employment rate was 31.6 percent. Therefore, the situation remained unchanged in the last three years observed. The Labor Force Survey does not recognize youth as a population category between 15 and 30 years of age, but provides data for the 15-24 age group. The unemployment rate for this category in 2015 was 62.3 percent, in 2014 it was 62.7 percent and in 2013 it was 59.1 percent. Looking a few years back shows a continuous increase of youth unemployment rate, which was 63.1 percent in 2012, 57.9 percent in 2011, 57.5 percent<sup>10</sup> in 2010, 48.7 percent in 2009 and 47.5 percent<sup>11</sup> in 2008. According to preliminary data of the Labor Force Survey, published in July 2016<sup>12</sup>, the unemployment rate of the general population was 25.4 percent. This is a decrease compared to the 2013-2015 period. The youth unemployment rate was 54.3 percent, which shows a decrease compared to 2015, but still the highest compared to all observed age categories. On the other hand, youth employment rates are very low compared to other age categories; 12.1 percent in 2015, 10.9 percent in 2014 and 11.6 percent in 2013. Comparing these percentages to indicators from other countries in Europe and the world paints an even clearer picture about the gravity of the problem. This is confirmed by the World Bank data<sup>13</sup>, calculated according to the International Labor Organization methodology, which shows that the 57.2 percent youth unemployment rate in Bosnia and Herzegovina in 2014 is the highest among the Western Balkans countries—50.2 percent in Macedonia, 49.5 percent in Serbia, 39.5 percent in Montenegro and 29.2 percent in Albania. Furthermore, the youth unemployment rate in BiH is the second highest among a total of 219 countries observed, second only to Spain whose unemployment rate was 57.9 percent, and followed by Greece with a 53.9 percent unemployment rate. The average youth unemployment rate for the 15-24 age group in the 28

<sup>9</sup> Agency for Statistics of Bosnia and Herzegovina, *Labour Force Survey 2015—Final Results*, 2015, [http://www.bhas.ba/ankete/ARS\\_2015\\_BiH.pdf](http://www.bhas.ba/ankete/ARS_2015_BiH.pdf).

<sup>10</sup> Agency for Statistics of Bosnia and Herzegovina, *Labour Force Survey 2012—Final Results*, 2012, [http://www.bhas.ba/ankete/lfs\\_bh.pdf](http://www.bhas.ba/ankete/lfs_bh.pdf).

<sup>11</sup> Agency for Statistics of Bosnia and Herzegovina, *Labour Force Survey 2010—Final Results*, 2010, [http://www.bhas.ba/ankete/lfs\\_2010\\_001\\_01-bh.pdf](http://www.bhas.ba/ankete/lfs_2010_001_01-bh.pdf).

<sup>12</sup> Agency for Statistics of Bosnia and Herzegovina, *Labour Force Survey 2016—Preliminary Results*, July 2016, [http://www.bhas.ba/ankete/LFS\\_saopcenje%20BOS.pdf](http://www.bhas.ba/ankete/LFS_saopcenje%20BOS.pdf).

<sup>13</sup> The World Bank, <http://data.worldbank.org/indicator/SL.UEM.1524.ZS>, accessed on September 21, 2016.

European Union member states was 22.2 percent in 2014, which is 2.8 times lower than Bosnia and Herzegovina's 62.7 percent<sup>14</sup> rate. Data on youth unemployment in Bosnia and Herzegovina can be analyzed in more detail and from different aspects, but due to limitations in scope and the different focus of this paper, only a few data points were presented to facilitate the general understanding of the problem.

Unemployment causes multiple negative consequences for the state and society, which are difficult to measure precisely in terms of expenses—as they primarily constitute the loss of revenue that unemployed persons would generate if employed, long-term loss of high-quality human resources due to unused skills and abilities becoming obsolete, poverty caused by low and limited in time unemployment benefits, decrease in revenues generated for the state through direct and indirect taxes, increase in crime rates, compromised mental and physical health of the unemployed, etc.<sup>15</sup> Gerard, Valsamis and Van der Beken<sup>16</sup> list three different costs of unemployment—costs for the individual, the government and the society. For the individual, unemployment can impact the standard of living, harm their mental and physical health and lower their life expectancy. The negative consequences on the society are reflected through an increase in crime rates and divorce, a marked difference in population income and a decrease in total consumption, etc. The costs of unemployment for the government are easier to measure and they concern the increase in public intervention for the purpose of encouraging employment and combatting unemployment, the potential loss of revenues generated for the state through taxes and salary contributions for the unemployed, additional administrative expenses in employment agencies, expenses for unemployment benefits given to the unemployed and the government's loss of indirect taxes caused by the fall in purchasing power of unemployed persons.

If we look at Bosnia and Herzegovina, in 2015, for instance, the funds allocated for the material and social security of unemployed persons, which include financial aid for the unemployed, obligatory health insurance, and retirement and disability insurance for persons with up to three years

---

<sup>14</sup> Eurostat, Enlargement countries—labour market statistics, [http://ec.europa.eu/eurostat/statistics-explained/index.php/Enlargement\\_countries\\_-\\_labour\\_market\\_statistics#Further\\_Eurostat\\_information](http://ec.europa.eu/eurostat/statistics-explained/index.php/Enlargement_countries_-_labour_market_statistics#Further_Eurostat_information), accessed on September 21, 2016.

<sup>15</sup> Horst Feldmann, "Economic Freedom and Unemployment", in James Gwartney Joshua Hall and Robert Lawson, *Economic Freedom of the World: 2010 Annual Report*, (Canada: Fraser Institute, 2010).

<sup>16</sup> Maarten Gerard, Daphné Valsamis and Wim Van der Beken, *Why invest in employment? A study on the cost of unemployment*, (Brussels: Idea Consult, 2012).

short of retirement age, amounted to 75.525.438,00 BAM<sup>17</sup> in FBiH, 16.997.546,61 BAM<sup>18</sup> in RS, and 1.119.211,00 BAM<sup>19</sup> in Brčko District. This amounts to a total of 93,642,195.61 BAM in costs the government had in 2015 for a certain number of unemployed persons with access to these rights. Analysis of a non-governmental organization Centers of Civic Initiatives<sup>20</sup> shows that entity employment bureaus spent a total of 89,400,000 BAM in the 2013–15 period (FBiH: 60,200,000 BAM and RS: 29,200,000 BAM) for active employment policies through independent programs, which is 30 million BAM annually, on average. This means that the costs for active employments policy measures, combined with unemployment benefits costs amount to 120 million BAM annually, without including other, previously listed and described, costs. Therefore, the state is at a multiple loss due to unemployment of all age categories. When it comes to youth, this loss is amplified by an additional, albeit hard to measure, factor which concerns untapped capacities, innovation and proactive attitudes new generations can offer.

## Unemployment as the Cause Behind Youth Leaving BiH

One of the consequences of unemployment plaguing Bosnia and Herzegovina, year after year, is the emigration of youth and other citizens to European Union member states, as well as beyond the European continent. Unfortunately, there is no centralized and unified source of data that would enable us to track this indicator at the annual level, or to monitor this trend.

One of the official sources is the Agency for Identification Documents, Registers and Data Exchange (IDDEEA), which monitors the number of cancelled permanent or temporary residence registrations in Bosnia and

<sup>17</sup> Federal Employment Bureau, *Izveštaj o radu Federalnog zavoda za zapošljavanje za 2015. godinu*, March 2016, [http://www.parlamentfbih.gov.ba/dom\\_naroda/bos/parlament/propisi/El\\_materijali\\_2016/Izvestaj%20o%20radu%20FZZZ%20za%202015.pdf](http://www.parlamentfbih.gov.ba/dom_naroda/bos/parlament/propisi/El_materijali_2016/Izvestaj%20o%20radu%20FZZZ%20za%202015.pdf).

<sup>18</sup> Public Institution Employment Institute of Republika Srpska, *Izveštaj o radu JU Zavoda za zapošljavanje Republike Srpske za 2015. godinu*, February 2016, [http://www.zzzrs.net/dokumenti/izvjestaj\\_o\\_radu\\_2015.pdf](http://www.zzzrs.net/dokumenti/izvjestaj_o_radu_2015.pdf).

<sup>19</sup> Employment Institute of Brčko District BiH, *Izveštaj o radu za 2015. godinu*, July 2016, [www.zzzbrcko.org/dokumenti/IZVJE%20C5%A0TAJ%20O%20RADU%20ZAVODA%20ZA%202015.%20GOD.P.doc](http://www.zzzbrcko.org/dokumenti/IZVJE%20C5%A0TAJ%20O%20RADU%20ZAVODA%20ZA%202015.%20GOD.P.doc).

<sup>20</sup> Centers for Civic Initiatives, *Reformska agenda i aktivne politike zapošljavanja u Bosni i Hercegovini—Da li vlade i zavodi zavode ili zapošljavaju nezaposlene?*, August 2016, [www.posaonarodu.ba/files/download/50/posao\\_narodu\\_policy\\_brief\\_engpdf](http://www.posaonarodu.ba/files/download/50/posao_narodu_policy_brief_engpdf).

Herzegovina for the purpose of emigrating into foreign countries, amounting to 3,948<sup>21</sup> in 2015. However, since the cancellation of residence is not required by law, a large number of persons leaving the country for employment or education elsewhere do not cancel their residence registration. Similar limitations are present in the data of the Agency for Labor and Employment, which records annual data on BiH citizens employed outside of BiH, but only for countries that signed employment agreements with Bosnia and Herzegovina. In 2015, there were 3,301<sup>22</sup> such individuals. However, this number is certainly higher because it does not include all the persons who found employment abroad by contacting employers directly, through employment mediation agencies, and in other ways.

The World Bank data is particularly valuable given the lack of domestic statistical data on emigration, and shows a 44.5 percent emigration rate in 2013, relative to the entire population of BiH, which ranks BiH as 16<sup>th</sup> out of a total of 214 observed countries and territories. Compared to countries in the region, Bosnia and Herzegovina is at the top spot when it comes to this indicator as well, since the rates for Serbia, Croatia and Albania are 18 percent, 20.9 percent and 43.6 percent, respectively.<sup>23</sup> According to data of the Union for Sustainable Return and Integration, more than 80,000 persons emigrated from BiH, evidenced by research conducted in local communities.<sup>24</sup>

One particularly worrying trend in Bosnia and Herzegovina is the emigration of citizens with university degrees, who leave in search of better opportunities—the so-called brain drain. This is also particularly characteristic of the youth population in BiH. Although theory and practice indicate that brain drain can have a positive effect, apart from the negative effect on the country citizens emigrated from, whether or not this applies to Bosnia and Herzegovina is debatable. According to World Bank data, the emigration rate for highly educated individuals in BiH is 23.9 percent, 11.1 percent of which are medical experts, which is one of the highest rates in the world.<sup>25</sup> According to the World Economic Forum data, BiH placed

---

<sup>21</sup> Ministry of Security, Sector of Immigration, *Bosnia and Herzegovina Migration Profile for the year 2015*, April 2016.

<sup>22</sup> *Ibid.*

<sup>23</sup> World Bank Group, *Migration and Remittances Factbook 2016, third edition.*

<sup>24</sup> Union for Sustainable Return and Integration, <http://www.uzopibih.com.ba/2016-04-14.html>, accessed on August 20, 2016.

<sup>25</sup> World Bank Technical Assistance Project P123211, *Overview of the Research and Innovation Sector in the Western Balkans*, October 2013.

as 136<sup>th</sup> out of 140 countries in terms of its capacity to retain talent in 2015, and 137 in terms of its capacity to attract talent.<sup>26</sup> In 2013, BiH placed as 143<sup>rd</sup> and 144<sup>th</sup>, respectively, out of a total of 148 countries.<sup>27</sup> The measurement methodology was somewhat different before 2013, and these two indicators were presented as one indicator called “brain drain”; therefore, in 2011, BiH was ranked 126<sup>th</sup> out of a total of 142 observed countries.<sup>28</sup> This data is easy to interpret and bears witness to the continued gravity of the brain drain problem in BiH.

UNDP’s “National Human Development Report 2002” indicates that 92,000 youth left BiH between 1991 and 2001.<sup>29</sup> Data provided by the Institute for Youth Development KULT shows that 150,000 young people left BiH between the end of the war and 2013. In the survey conducted by the Institute, 60 percent of youth in F BiH said that they want to leave BiH to find employment abroad, in more promising and economically stronger countries. The reasons listed for leaving include corruption, unemployment, low standard of living and an unpromising future. As many as 37 percent of youth would move abroad permanently if given the opportunity, and 9 percent have already taken concrete steps towards leaving the country. This survey also revealed that more than half of BiH youth had neighbors who left the country in the last 7 years, 45 percent of youth have a member of their extended family who left the country, and 26 percent have a member of their immediate family who left the country in the last 7 years.<sup>30</sup>

Similar data was yielded by the “Voices of Youth” survey conducted within the 2012 UN Youth Employability and Retention program.<sup>31</sup> 53.3 percent of young respondents stated that they would definitely leave BiH to pursue their studies, if given the opportunity. This percentage is higher than the 46 percent from 2008. 65.6 percent of respondents would leave the country for temporary work, which is an increase of almost 10 percent from the 55.1 percent in 2008, and 52.3 percent (compared to 46 percent

---

<sup>26</sup> Schwab, K., *The Global Competitiveness Report 2015-2016*, (Geneva: World Economic Forum, 2015).

<sup>27</sup> Schwab, K., *The Global Competitiveness Report 2013-2014*, (Geneva: World Economic Forum, 2013).

<sup>28</sup> Schwab, K., *The Global Competitiveness Report 2015-2016*, (Geneva: World Economic Forum, 2011).

<sup>29</sup> United Nations Development Program, *National Human Development Report Bosnia and Herzegovina 2002*, 2002.

<sup>30</sup> Institute for Youth Development KULT, *op.cit.*

<sup>31</sup> United Nations Development Program, *op.cit.*

in 2008) would leave to live in another country, and 41 percent (34.1 percent in 2008) for marriage. A little over one third of respondents (38.1 percent compared to 36.9 percent in 2008) would move abroad for a longer period (or permanently) 42.9 percent (compared to 29.8 percent in 2008) would move abroad for a longer period, but not permanently. It is quite concerning that only a little less than one fifth of the respondents (18.9 percent, compared to 20.3 percent in 2008), stated that they would not leave BiH for a longer period or permanently, i.e. the fact that most youth would actually like to leave this country is cause for concern.

This data is not new, since the first survey on youth emigration in the post-war period was conducted by the UNDP, followed by a report in 2000, called “National Human Development Report on Youth”. The report stated that 62 percent of youth would leave Bosnia and Herzegovina if given the opportunity.<sup>32</sup> Therefore, as early as 2000, the government, society and the public were sent a clear and alarming signal about this problem by the youth themselves. We can note that after about 10 years the aspirations of youth in BiH have remained nearly identical, with many having acted on their aspirations in the meantime and left the country. This is partly a consequence of the difficult economic situation in the country, as well as a reflection of the government’s inadequate treatment of this problem. This begs the question: how is it possible that we are allowing for a continuous mass exodus of a highly-qualified workforce that should be treated as the key potential for the development of any country? In the case of Bosnia and Herzegovina, a developing country, a country engaged in reform processes, a country whose economy, education system and science are struggling to survive, a country that needs individuals with above-average capacities and achievements who are capable of shouldering the weight of these processes, addressing this issue becomes even more paramount.

Research shows that the most common factors affecting brain drain are connected with the socioeconomic and political situation in the country, such as political instability, high unemployment rates and war, violation of human rights and workers’ rights, lack of academic freedom and poor management decisions.<sup>33</sup> On the other hand, countries that offer solid

---

<sup>32</sup> United Nations Development Program and Independent Bureau for Humanitarian Issues, *Human Development Report Bosnia and Herzegovina 2000 Youth*, 2000.

<sup>33</sup> Sara Nikolić, Borića Mraović and Emina Čosić, *Brain Gain: Kako vratiti, zadržati i dovesti stručnjake u BiH?*, (Sarajevo: Association Alumni of the Center for Interdisciplinary Post-graduate Studies (ACIPS), 2010), <http://grupa484.org.rs/wp-content/uploads/2012/09/Brain-Gain-Kako-vratiti-zadržati-i-dovesti-strucnjake-u-BiH-ACIPS-2010.pdf>.

income, employment and opportunities for professional development and networking, and, ultimately, a positive social, economic and political environment, attract highly qualified migrants.<sup>34</sup> Numerous statistical data testify to the unfavorable and discouraging socioeconomic and political environment, employment opportunities and career progress in BiH, which clearly points to the direction that the government and the society should take.

### **Where Are the Youth in the Reform Agenda?**

The “Reform Agenda for Bosnia and Herzegovina 2015–18” is a document reflecting BiH’s strategic commitment to overcome the difficult socio-economic situation in the country, and meet all the conditions for becoming an EU member state. As stated in the document, the government recognized “an urgent need to initiate the process of rehabilitating and modernizing the economy with a view to: fostering sustainable, efficient, socially just and steady economic growth; creating new jobs; increasing and more-appropriately targeting social assistance; and creating a favorable and just social environment.”<sup>35</sup> Government representatives emphasize in their public statements that this is a set of medium-term priorities intended to galvanize comprehensive structural reforms in the areas of labor legislation, public administration, employment policies in the public sector, business environment and competitiveness, restructuring of public companies, social welfare, the health sector and the rule of law, in order to sustain macroeconomic stability and encourage growth and competitiveness.

The Reform Agenda was adopted in July 2015 by the Council of Ministers of Bosnia and Herzegovina, the Government of the Federation of Bosnia and Herzegovina and the Government of Republika Srpska, and in November 2015 by the Government of Brčko District. This is another fact that government representatives often emphasize during their media appearances—there is finally one harmonized document at the level of Bosnia and Herzegovina, and a common commitment on all government levels to making progress. It can be noted that this emphasis is somewhat understandable, having in mind the complex political and administrative system in Bosnia and Herzegovina, which frequently hindered the process

---

<sup>34</sup> Nikolić, Mraović and Ćosić, *op.cit.*

<sup>35</sup> Reform Agenda for Bosnia and Herzegovina 2015–2018, p. 1, <http://europa.ba/wp-content/uploads/2015/09/Reform-Agenda-BiH.pdf>.

of joint strategic decision making and activities. That is why expectations from the Reform Agenda are much higher than from any strategies, plans, programs, decisions and similar documents developed thus far, although their importance is unquestionable. Furthermore, the numerous negative economic and social indicators in BiH make it abundantly clear that the Reform Agenda is inevitable and bound to be implemented dynamically. The adoption of the Reform Agenda was followed by the development of Action Plans for the implementation of the Reform Agenda by the aforementioned levels of governments, and cantonal authorities in the Federation of BiH have accepted this same obligation. The Reform Agenda includes the implementation of a set of reforms in six key sectors: public finance, taxes and fiscal sustainability; business environment and competitiveness; labor market; social protection and pension system reform; the rule of law and good management; public administration reform. Action Plans by the Council of Ministers of BiH, Federation of BiH and the Government of RS for the implementation of the Reform Agenda contain a total of 172 measures, 33 of which belong to the Action Plan of the Council of Ministers, 61 to the Government of FBiH and 78 to the RS Government.

In the context of youth and the Reform Agenda, it is important to note that the development and adoption of the Reform Agenda was preceded by the publication of a document titled “Compact for Growth”, which certainly influenced the content of the Reform Agenda. This Compact was published in 2014, at the initiative of the Office of the EU Special Representative in Bosnia and Herzegovina, and comprises a set of recommendation borne out of the Forum for Prosperity and Employment held at the end of May 2014. This Compact defined employment and youth employment as one of the 6 proposed reform areas, stating that “Bosnia and Herzegovina needs to enact a set of labour market reforms to increase job creation, including by revitalizing the process of collective bargaining, reducing the disincentives for hiring and, in particular, promoting inclusion of the young population in the workforce.”<sup>36</sup> Therefore, the labor market is the area wherein the Reform Agenda laid out measures directly targeting youth.

More specifically, the Action Plan of the Government of the Federation of Bosnia and Herzegovina<sup>37</sup> contains a measure for adopting and imple-

---

<sup>36</sup> Compact for Growth and Jobs in Bosnia and Herzegovina, [http://europa.ba/wp-content/uploads/2015/05/delegacijaEU\\_2014090816171626eng.pdf](http://europa.ba/wp-content/uploads/2015/05/delegacijaEU_2014090816171626eng.pdf).

<sup>37</sup> Government of the Federation of Bosnia and Herzegovina, *Ažurirani akcioni plan za realizaciju Reformske agende Federacije Bosne i Hercegovine*, December 2015, [http://www.fbihvlada.gov.ba/pdf/Akcioni%20plan\\_azurirani.pdf](http://www.fbihvlada.gov.ba/pdf/Akcioni%20plan_azurirani.pdf).

menting a Directive on Incentivizing Employment. The Directive is aimed at stimulating first employment and self-employment of youth without work experience, with subsidized expenses concerning the relevant salary contributions, which the government of FBiH will fund with 50 million BAM. This measure, as such, is an active employment measure. Pursuant to the Directive adopted in December 2015, in February 2016 a Request for Applications was published for submitting requests for subsidizing first employment and self-employment. The funds for first employment are used by employees from the private sector, engaged in activities that are not related to trade, the hospitality sector or organizers of games of chance, employing unemployed persons in the 15-30 age range without work experience in the profession they were educated for. The beneficiaries of self-employment funds are unemployed persons over the age of 18, who registered their own business after the Directive came into force. The subsidy is paid to the employer for the purpose of a reimbursement in the amount of a minimum salary in FBiH, salary contributions corresponding to the minimum salary in FBiH and income tax for the newly employed, or the self-employed. The subsidies are given for the first year of the unemployed person's pensionable service, with the proviso that the employer is required to keep the person employed for the following year without subsidies, i.e. while complying with the obligation to pay the employee's salary and contributions. This provides youth with their first two years of work experience. It is particularly important for youth, having in mind the difficulty of finding their first job in Bosnia and Herzegovina, which often leads to long-term unemployment, late start to careers, career discontinuity, social exclusion, etc. The implementation of the Directive actually encourages employers to hire, and offers support to new businesses immediately upon launching. At the time of writing this paper, according to the data available on the website of the Federal Employment Institute, 1,763 employers and 2,255 individuals with new businesses applied to the Request for Applications.<sup>38</sup> In public statements, representatives of the Government of FBiH state that there are approximately 7,200 potential new employees, since some employers applied to receive subsidies for multiple employees. Those who applied are expected to sign contracts in the upcoming period.

It is important to note that this type of active employment policy measure is being implemented for the first time in the Federation of BiH, and

---

<sup>38</sup> Federal Employment Bureau, <http://www.fzzz.ba/projekti/uredba-subvencioniranje-zapoljanja-mladih-bez-radnog-iskustva-i-samozapoljavanja>, accessed on Spetember 21, 2016.

the entire BiH. This means there is a risk of failure and not achieving the desired effects. It is therefore important to continuously monitor the implementation of the Decision for the two years during which the Government of FBiH will be providing financial support to employers and entrepreneurs, and to extend this monitoring process beyond this period in order to measure its long-term effects. Long-term monitoring must not be neglected, having in mind the amount of funds allocated for implementing this measure, and the announcement by the Government of FBiH regarding the increase of funds over the following years with the aim of reaching as many unemployed persons as possible.

The labor market section of the Action Plan of the Government of Republika Srpska for the Implementation of the Reform Agenda<sup>39</sup> contains a measure called “Introducing support schemes for persons seeking first employment.” Since a more detailed elaboration could not be found, it is assumed that the intentions of the Government of Republika Srpska are similar to those of the Government of FBiH, in terms of addressing unemployment. The Action Plan states that the measure will be implemented during 2016. According to the results of the Independent Monitoring of Implementation and Efficiency of the Reform Agenda for Bosnia and Herzegovina 2015–18<sup>40</sup>, conducted by the Centers of Civic Initiatives and published at the end of May 2016, this measure has not yet been implemented.

Other measures from the action plans for implementing the Reform Agenda should indirectly improve youth conditions for employment and the conditions for already employed youth, through a reform of the education system which is intended to align education with the labor market, as well as through improving the labor law draft, increasing the flexibility of working conditions, differential, efficiency-based calculation of salaries, separating obligatory health insurance from employment mediation, etc.

The government’s commitment to addressing youth issues is evidenced by the strategic documents, laws, plans, programs, and, even more specifically, through allocating budget funds for youth issues. Results of research conducted by the Agency for Local Development Initiatives in BiH<sup>41</sup>

---

<sup>39</sup> Government of Republika Srpska, *Akcioni plan Republike Srpske*, [http://www.vladars.net/sr-SP-Cyrl/Documents/Akcioni\\_plan\\_Republike\\_Srpske\\_211215.pdf](http://www.vladars.net/sr-SP-Cyrl/Documents/Akcioni_plan_Republike_Srpske_211215.pdf).

<sup>40</sup> Centers for Civic Initiatives, *Independent Monitoring of Implementation and Effectiveness of “Reform Agenda of Bosnia and Herzegovina for the period 2015-2018”—State of Nation, report 2*, May, 2016, [www.posaanarodu.ba/files/download/48/state\\_of\\_nation\\_report\\_2pdf](http://www.posaanarodu.ba/files/download/48/state_of_nation_report_2pdf).

<sup>41</sup> Agency for Local Development Initiatives, *Finansijsko lice politike u Bosni i Hercegovini*, September 2010, [http://www.aldi.ba/files/ALDI%20Analiza2007\\_2010\\_FINAL.pdf](http://www.aldi.ba/files/ALDI%20Analiza2007_2010_FINAL.pdf).

show that in budgets of the institutions in of BiH, FBiH, Republika Srpska and all ten cantons in FBiH, in the 2007–10 period, 14 million BAM was allocated for improving the position of youth. In terms of total funds allocated for improving the position of youth, relative to the total budget, the highest amount of funds for improving the position of youth in the observed period was allocated in 2007, and comprised 0.10 percent of the total budget costs, and the lowest amount of funds was allocated in 2010, when it amounted to 0.03 percent of total budget costs. It is also important to note that funds allocated for youth decreased from 5.2 million BAM in 2006 to 2.2 million BAM in 2010, or by 58 percent.

According to data yielded by the analysis of the FBiH budget, conducted by the Institute for Youth Development KULT with a focus on youth, by using information available to the public on websites of relevant ministries, youth were allocated 1,714,000 BAM in 2015, which is 0.07 percent of the total FBiH Budget for 2015. For the sake of comparison, in 2014, 2,298,700 BAM was allocated from the FBiH Budget, which comprised 0.10 percent. The execution percentage for funds allocated for youth was around 99 percent in 2014 and 90 percent in 2015. The Report on the 2014 FBiH Budget execution does not offer disaggregated data for any category of the society, including youth. Youth, youth organizations, and organizations concerned with youth issues would find it very useful if the Report on FBiH Budget Execution recognized youth as a distinct category and provided data on funds allocated for youth. The allocated funds include scholarships for different youth categories, training young public servants, youth tourism, youth entrepreneurship, scholarships for training youth in old crafts, etc. The data showing budget funds allocations for youth prove that these funds are very scarce, and have been declining over the years.

### **How and to What Extent Are Youth Involved in Decision Making and Implementing Reform Processes in BiH?**

As noted previously, the Youth Law of the Federation of Bosnia and Herzegovina, and the Law on Youth Organizing of Republika Srpska define the rights and obligations of youth in BiH. The fact that these laws exist is commendable, because their adoption in 2010 (FBiH) and 2004 (RS) provided youth with a legal framework defining their age and the various mechanisms for youth work, and obligated all levels of government to care for youth, while also providing them with precise ways of doing

so, and essentially regulating the area of youth organization through youth associations and their representative bodies, in addition to other issues.

The Guide to the Youth Law in FBiH states that this law guarantees youth participation in bodies representing youth, primarily youth councils at the local, cantonal and federal level. Through these bodies, youth will be able to participate in decision-making processes, creating youth policies and strategies and in other processes that concern them.<sup>42</sup> Prior to the adoption of the Youth Law of FBiH, youth in this entity did not have their legal representatives, which prevented them from presenting their needs, problems and demands directly to government representatives. The Law stipulates the founding of youth councils at the local, cantonal and federal level. From 2010 to 2016, the implementation of the Law resulted in the founding of the Youth Council of the Federation of BiH in 2015, 6 cantonal councils and several local youth councils.

The key stage of the process of implementing the Law—the adoption of the Youth Strategy of FBiH—has not been implemented as of yet. The Strategy has been developed and is currently waiting to be adopted by the Government of the Federation of BiH. While the Youth Law of FBiH is the cornerstone for the development of a higher quality youth policy by the federal authorities, the adoption of the Youth Strategy would lay the groundwork for specific activities relevant to youth needs. Furthermore, the Law stipulates that “municipal, city and cantonal government authorities shall establish a youth committee as part of the municipal council as a permanent working body or of the cantonal assembly, which deals with youth issues as part of its competence, and includes representatives from the municipal or cantonal youth council.”<sup>43</sup> One of the obligations stipulated by the Law that has a satisfactory implementation dynamic is the training of youth officers. Another important stipulation of this Law is the founding of the Council for Youth of FBiH as an inter-ministerial working body, with 50 percent of its membership being representatives of the Youth Council of the Federation, which has not been implemented as yet.

The Law on Youth Organizing of Republika Srpska stipulates that the competent organs of RS, cities and municipalities are required to form special commissions for youth, by “selecting members of the commissions from the youth councils of Republika Srpska, cities or municipalities and

---

<sup>42</sup> Jasmin Bešić and Rusmir Pobrić, *Vodič kroz Zakon o mladima Federacije Bosne i Hercegovine*, (Sarajevo: Institute for Youth Development KULT, 2011).

<sup>43</sup> Youth Law of the Federation of Bosnia and Herzegovina, *op.cit.*, p.12

representatives of the legislative branch of government in Republika Srpska, cities and municipalities.”<sup>44</sup> The Law stipulates the development of the Youth Policy of Republika Srpska, defined at the level of Republika Srpska, cities and municipalities for the short-term (annual) and medium-term (five years) youth policy period at the level of Republika Srpska, cities and municipalities. The Law stipulates that “the Youth Policy of Republika Srpska for the short-term is developed by the Government of Republika Srpska, as proposed by the Ministry of Education and Culture, with active participation of youth representatives.” The medium-term youth policy for Republika Srpska is passed by the National Assembly of Republika Srpska, and proposed by the Ministry of Education and Culture. The medium-term and short-term youth policy plan is developed for a city or municipality, by the city or municipal assembly and is proposed by the competent youth commission, with the participation of the municipal or city youth council. A certain number of the commission members are members of the Assembly, while the remaining members are representatives of youth organizations.”<sup>45</sup> Therefore, youth participation in planning and decision-making processes is guaranteed by Law. Thus far, the Youth Policy of Republika Srpska was adopted for the 2006–10, 2010–15 and 2016–20, complete with action plans. Furthermore, the Youth Council of Republika Srpska was formed as the umbrella youth organization in Republika Srpska, whose membership includes local and RS level youth organizations, so that their interests are represented in front of the institutions of Republika Srpska.

It is clear that youth participation in the process of strategic decision making on issues of interest to youth was secured in Republika Srpska much earlier than in the Federation of BiH. It is also evident that youth issues are more specifically addressed there, which is evidenced by the three adopted entity strategies, i.e., youth policies and the fact that the first youth policy was adopted within a year of the law being passed, compared to the Federation where this has still not been done, even after 6 years. Does this put youth in Republika Srpska in a better position than youth in the Federation of BiH? What about youth in Brčko District who do not have any kind legislation dedicated exclusively to their rights and obligations? It is hard to say, given the fact that many indicators, such as the brain drain indicators, can be tracked only at the state level, and considering the numerous factors affecting the measuring of the same indi-

---

<sup>44</sup> Law on Youth Organizing of Republika Srpska, *op.cit.*, p.6

<sup>45</sup> *Ibid.*, p. 3

cators in both entities, effectively hindering data comparability. It would certainly be interesting to research and measure quantitatively whether the passing of both laws improved the economic and social position of youth.

Youth are a significant part of the electorate in Bosnia and Herzegovina. During general elections in 2006, youth participated in the electorate with 20.11 percent, in 2010 with 20.13 percent and in 2014 with 17.18 percent. Youth turnout during general elections was 51.35 percent in 2006 (304,152 youth), 52 percent in 2010 (356,291 youth) and 51.64 percent in 2014 (319,464 youth).<sup>46</sup> This data shows that youth play an active part in the process of electing political representatives, which disproves the public opinion of youth as inactive and uninterested. The potential power of the youth vote is illustrated by the fact that the political party that won the elections had approximately 250,000 votes, while youth turnout was around 300,000 of a total of around 600,000 youth of voting age. An analysis of a survey on youth electorate turnout in BiH in 2014<sup>47</sup> showed that the majority of political parties who ran during the general elections held in 2014 did not have a specific program for youth. Out of a total of 65 political parties registered for the elections, only 14 parties had a chapter dedicated to youth within their official programs, whereas 51 political parties mentioned youth sporadically, or not at all. Youth are mostly accorded only a few sentences in parts of the programs dealing with education, and even less than that in segments elaborating on employment policies, and, very rarely, in issues of falling birth rates and housing issues. On the other hand, youth have the option of becoming active in political parties, which may lead to them making decisions on strategic issues by participating in councils at the local level, assemblies at the cantonal level, parliaments at the entity and state levels. The level of political participation of youth in BiH is still very unsatisfactory, which is illustrated by the fact that 8 percent of youth were members of political parties, or youth wings of political parties in 2008.<sup>48</sup> The data for 2012 are very similar; 9.1 percent of youth were members of political parties and 5.8 percent of youth were members of youth wings of political parties.<sup>49</sup>

---

<sup>46</sup> Central Election Commission, *Izborni pokazatelji 2002-2014. godina*, February 2015, [https://izbori.ba/Documents/2015/25052015/Izborni\\_Pokazatelji\\_2002-2014.pdf](https://izbori.ba/Documents/2015/25052015/Izborni_Pokazatelji_2002-2014.pdf)

<sup>47</sup> Šherzada Halimić, *Mladi i izbori—Analiza istraživanja o učešću mladih na izborima u BiH 2014*, (Sarajevo: Institute for Youth Development KULT, 2014).

<sup>48</sup> Commission for Coordination of Youth Issues in BiH and German Society for International Cooperation GIZ, *op.cit.*

<sup>49</sup> United Nations Development Programme, *op.cit.*

July of 2016 saw progress for youth in the Western Balkans as well as for the youth in Bosnia and Herzegovina. During the Western Balkans Leaders' Summit, held in Paris on July 4, the Regional Youth Cooperation Office (RYCO) was formally founded through an international agreement signed by the presidents of Albania, BiH, Montenegro, Macedonia, and Serbia. The Office will consist of representatives of the governments and the civil sector of these six countries. It is presumed that the civil sector will be represented by youth organizations and associations, i.e. youth. The primary function of the Office will be the implementation of exchange programs, with the aim of contributing to mobility, intercultural learning and reconciliation of youth in the region. The existence and membership structure of the Office sends an encouraging message about the official cooperation of the government and non-governmental sector for the benefit of youth, and the strengthening of the connection among countries in the region in their joint efforts to overcome challenges related to youth issues that are shared by all these countries. "Promoting youth employment and entrepreneurship by presenting models of good practices from the region, as well as encouraging mobility to gain work experience/vocational training and employment" are listed among the goals that inspired its founding, in the "Joint Declaration on the Establishment of the Regional Youth Cooperation Office in the Western Balkans,"<sup>50</sup> signed in August 2015, prior to the formal establishment of the Office.

## Conclusion

Finally, it is important to consider once more what youth represent for society. Several authors<sup>51</sup> say there are two approaches: treating youth as a resource, and treating them as a problem. The approach that treats youth as a resource entails seeing youth as representatives of the future, the source of innovation, the purveyors of dominant social values that are passed from generation to generation, and are actually a rare resource. Approaching youth as a problem entails a negative perception of youth as

<sup>50</sup> Joint Declaration on the Establishment of the Regional Youth Cooperation Office of the Western Balkans, Vienna Western Balkans Summit 2015, p. 3, [https://rycoblog.files.wordpress.com/2015/12/annex\\_1\\_jointdeclaration\\_establishment-youth-cooperation-office-western-balkans-1.pdf](https://rycoblog.files.wordpress.com/2015/12/annex_1_jointdeclaration_establishment-youth-cooperation-office-western-balkans-1.pdf)

<sup>51</sup> Vlasta Ilišin and Vedrana Spajić Vrkač, *Potrebe, problemi i potencijali mladih u Hrvatskoj*, (Zagreb: Ministry of Social Policy and Youth of the Republic of Croatia, 2015), [www.mspm.hr/UserDocsImages/MLADI/potrebe-problemi-i-potencijali-mladih-u-Hrvatskoj-istrazivacki-izvjestaj.docx](http://www.mspm.hr/UserDocsImages/MLADI/potrebe-problemi-i-potencijali-mladih-u-Hrvatskoj-istrazivacki-izvjestaj.docx).

a population group in a delicate development stage, prone to deviant behavior, along with an obvious distrust towards youth and a negative view of their marginalized social status. It is difficult to state conclusively which of the two aforementioned applies to the status of youth in BiH. Youth comprise almost one fifth of the population in BiH. Research, analyses and studies point to their unfavorable economic and social position. Youth themselves are making this obvious, both with words, and by their actions of leaving the country to seek employment or education elsewhere. Whether or not they will come back is questionable, given the fact that the process of economic recovery is very slow. BiH has one of the highest rates of unemployment and brain drain in Europe and the world. Over the last few years, the government acknowledged youth rights by adopting a youth law, which is encouraging. On the other hand, in terms of budget funds for youth, the government is not showing a strong commitment to meeting their needs. Another encouraging development is the Reform Agenda and its action plans. However, it is still not clear whether unemployment—youth's biggest problem—will be solved and when. All that has been said thus far inspires several questions and thoughts. If the reform processes are being implemented to keep youth who want to leave the country, and to encourage youth who left to return, what happens if the reforms are not implemented completely? Or if they are not implemented quickly enough? Or if they are not implemented successfully, and do not yield the expected results? Can youth wait for dignity and happiness? Or is our youth leaving to other countries never to return again? What does this specifically mean for the present and future of Bosnia and Herzegovina? The situation is serious enough to compel the authorities and the society to ask these questions every day, and to be persistent in raising consciousness and the search for answers.



*Part III*

**Electronic Payments  
and Other Reforms**



## *Chapter 11*

# **Energy Efficiency Investment Benefits and How to Achieve Them: The Energy Efficiency Obligation (EEO)**

*Jane Wilson and Mak Kamenica*

The benefits of investing into energy efficiency measures are clear and have been proven by numerous pilot projects and activities in Bosnia and Herzegovina and through extensive international experience. In addition to the numerous benefits to citizens and businesses in BiH, as of October 16, 2015, the Energy Efficiency Directive<sup>1</sup> became obligatory for the Energy Community (EnC) Contracting Parties, including Bosnia and Herzegovina. The directive stipulates that the Contracting Parties must notify the EnC as to what energy efficiency policy measures they plan to adopt by October 15, 2017. The EE Directive requires all EnC Countries to set a savings target for an Energy Efficiency Obligation (EEO) model of at least 0.5 percent reduction of energy use in 2017 and 2018, and 0.7 percent in 2019 and 2020, or opt for alternative measures that show that the same targets will be achieved.

This paper proposes reaching the necessary investment values through the development of a market-based instrument for financing energy efficiency measures—the EEO. This mechanism obligates the companies supplying energy to customers to also invest in their customers' energy savings, and 52 such mechanisms functioning across the globe demonstrate that it is a very effective tool.

Some of the economic benefits that are analyzed in this paper, resulting from investing 100 million BAM annually<sup>2</sup> into energy efficiency measures in a systematic way are:

- Bosnia and Herzegovina's GDP could be increased by 370 million BAM annually, which in turn means:
  - 81 million BAM additional revenues from direct and indirect taxes

---

<sup>1</sup> European Union Directive, 2012.

<sup>2</sup> 100 million BAM annual investments into energy efficiency is used as a reference point in this paper for the calculations.

- 58 million BAM additional income from social security contributions
- 4,900 new full-time jobs could be created annually
- The demand for materials and equipment, such as windows, could double or even triple in BiH
- Energy security could be increased. The annual energy savings would be equivalent to the annual electricity usage of 17,000 average BiH households
- The amount of CO<sub>2</sub> emissions reduction equivalent to the annual emissions of 19,000

Energy efficiency (EE) is the most cost-effective way to save energy and reduce greenhouse gas emissions; as a result, increasing energy efficiency should be included in a country's energy policy. The implementation of EE measures saves money for end consumers, who can then spend the saved funds on other needs. Also, energy security is increased because the overall need for energy is reduced. EE will have an economic impact on the country because it will transform the energy market by creating employment and business development opportunities. The investment potential for energy efficiency measures in Bosnia and Herzegovina (BiH) is close to 5 billion BAM; this amount will achieve the planned savings included in the National Energy Efficiency Action Plan and fulfill the current Energy Community requirements for BiH.

Bosnia and Herzegovina is among the least energy-efficient states in Southeast Europe. Its energy bill was 2.1 billion euros in 2008, which represents almost 20 percent of the country's GDP. This is three times more than in the U.S. or EU.<sup>3</sup>

To begin the process of reducing this ratio of energy use to GDP in BiH by initiating the process of EE market transformation in Bosnia and Herzegovina and enabling sustainable energy development, it is necessary to develop a market-based instrument to provide mechanisms to stimulate the implementation of energy efficiency measures.<sup>4</sup>

This paper presents one market-based instrument—the Energy Efficiency Obligation Scheme—and the benefits to BiH of implementing it.

<sup>3</sup> UNDP BiH reports [http://www.ba.undp.org/content/bosnia\\_and\\_herzegovina/en/home/ourwork/environmentandenergy/successstories/sustainable-energy-solutions/](http://www.ba.undp.org/content/bosnia_and_herzegovina/en/home/ourwork/environmentandenergy/successstories/sustainable-energy-solutions/).

<sup>4</sup> International Energy Agency (IEA), *Market Based Instruments for Energy Efficiency, Policy Choice and Design*, Insight Series 2017. There are three basic energy efficiency

It is important to note that the total amount of investment generated by all market-based instruments has increased six-fold over the last ten years.<sup>5</sup>

## What is the Overall Investment Potential of Energy Efficiency in BiH?

The National Energy Efficiency Action Plan for BiH envisages the implementation of a series of programs to increase energy efficiency and achieve energy savings in primary (generation and distribution) and final consumption. In order to achieve the planned savings and reach the current requirements of the Energy Community for BiH, approximately 5 billion BAM in total should be invested into energy efficiency measures.<sup>6</sup> This investment means the development of industries related to the implementation of energy efficiency measures, new employment possibilities, energy savings, air pollution reduction and numerous other benefits. Figure 1 shows the most important benefits of energy efficiency measures that reveal a broad range of potential positive impacts.<sup>7</sup>

The data in the table below gives an indication of the number of years it would take to actually reach the 5 billion BAM investment for energy efficiency measures based on various examples of annual investment levels (targets).

From Table 1 we see that significant annual investments are required in energy efficiency measures to reach the targets within a reasonable time frame. In addition, before setting the annual investment target, an analysis of the energy efficiency materials and services supply chain capacity and its geographical coverage of the country should be carried out in order to make sure that the local economy reaps the most benefits from the implementation of EE measures. The supply chain needs time to develop and may not be able to provide sufficient energy efficiency measures initially

---

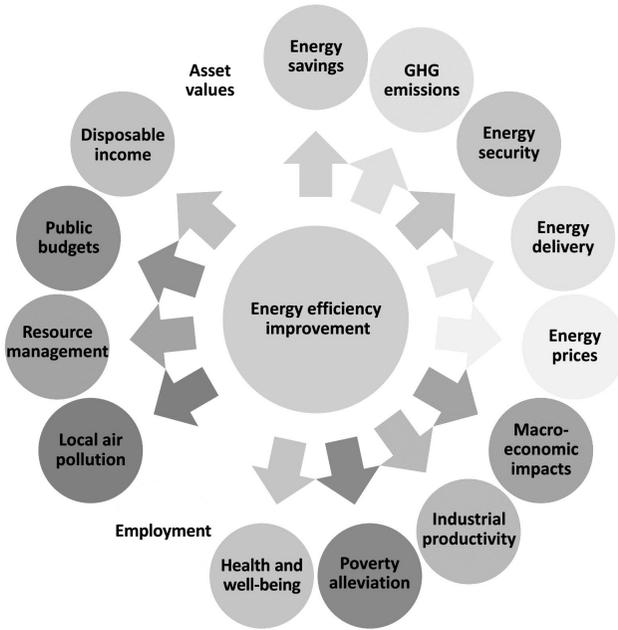
market-based instruments: auctions, white certificates and utility energy efficiency obligations (EEOs). <https://www.iea.org/publications/insights/insightpublications/market-based-instruments-for-energy-efficiency.html>.

<sup>5</sup> *Ibid.*

<sup>6</sup> The EU requirements are defined in the Energy Efficiency Directive (2012/27/EU), <https://www.energy-community.org/legal/acquis.html>. The requirements have been further quantified for Bosnia and Herzegovina in the draft National Energy Efficiency Action Plan, which has been used to approximate the investment potential.

<sup>7</sup> Figure 1.1 The multiple benefits of energy efficiency <https://www.iea.org/publications/freepublications/publication/capturing-the-multiple-benefits-of-energy-efficiency.html>.

**Figure 1. The Multiple Benefits of Energy Efficiency**



to meet a very high target. If this is the case, the targets can be increased over time in line with the achievable implementation rate.

**How to Finance Energy Efficiency Measures?**

A strategic approach to energy efficiency is needed, which requires the creation of financing mechanisms, implementation mechanisms and mechanisms for monitoring the results and quality of implemented energy efficiency measures.

**Table 1. Investments and Time Needed to Reach the EE Potential in BiH**

Annual investments	Years needed to reach the 5 billion KM potential
10 million BAM	500 years
100 million BAM	50 years
250 million BAM	20 years

Financing energy efficiency measures can be done in several ways, and there is no single best practice, as countries have developed their own individual approaches. Financing of energy efficiency measures is usually done through one of the following three ways: 1) government budget expenditures, 2) bank loans, or 3) market-based instruments. In developing countries such as BiH, financing through government expenditures would not be sufficient for the levels of investments needed. Financing energy efficiency through bank loans also has its drawbacks, as citizens and public institutions have other needs that are a higher priority than energy efficiency. Market-based instruments by themselves only set a policy framework specifying the outcome (e.g., energy savings) to be delivered by market actors; they do not describe the delivery mechanisms. One of the three market-based instruments for financing energy efficiency measures is the Energy Efficiency Obligation Scheme (EEO).<sup>8</sup>

## **Background on Energy Efficiency Obligation (EEO) Schemes**

One of the benefits of the EEO is that it involves the companies supplying energy to customers in the process of saving energy, which is not the case with most other energy efficiency programs. Once a country chooses an EEO as its market-based mechanism and sets the policy for the implementation of energy efficiency measures, then the process for actually implementing the EEO can start.

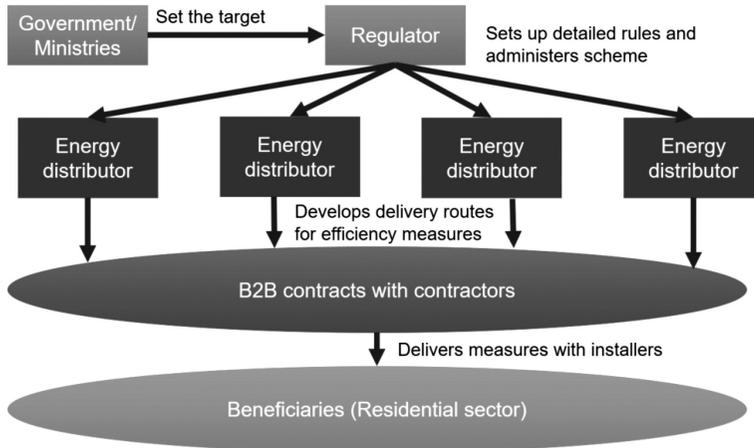
EEO schemes are market-based instruments that require obligated parties (energy distributors and/or suppliers) to deliver a specified amount of energy savings at the customer end within prescribed time periods. The obligated parties partially or fully fund energy efficiency measures for the end users to achieve the targeted amount of savings, and they recover the costs through energy prices. In other words, all energy customers pay an EEO fee, and the selected beneficiaries receive a subsidy for their energy efficiency works. Figure No. 2 below illustrates the EEO administrative process that has been defined through the BiH EEO Working Group.<sup>9</sup>

The EEO Scheme defines the financial mechanism(s) that can be implemented to reach the set targets. It also defines the procedures for monitoring, verification and reporting the achieved energy savings, which

---

<sup>8</sup> International Energy Agency, *op cit.*, Footnote 3.

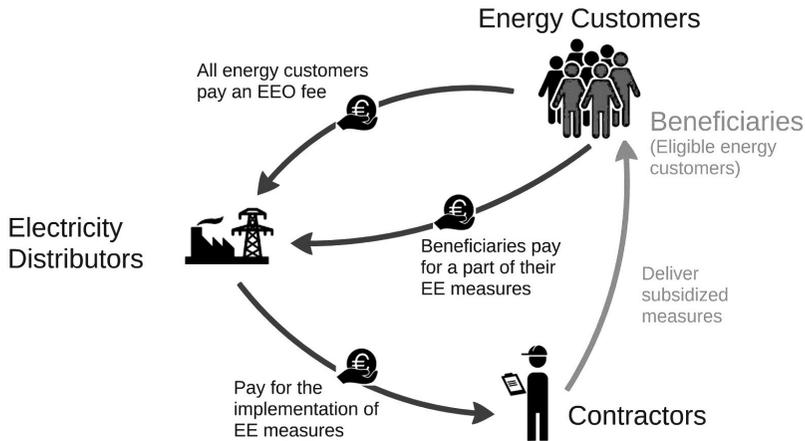
<sup>9</sup> See the Annex for more information on the BiH EEO Working Group and the BiH EEO formation steps that have been addressed.

**Figure 2. EEO Administrative Architecture**

confirm that the activities actually took place. The EEO schemes are typically enforced based on legislation and regulation that prescribe financial penalties for parties that do not comply.

EEO schemes have proven to be an excellent way not only to generate funds for EE measures but also to stimulate the economy of the countries that implement them. Through this market-based instrument, energy efficiency measures are financed on a large scale through a domestic financing source that does not depend on donor funding or loans. In addition, EEOs set a clearly defined target that provides certainty, increasing investor and business confidence. This has far-reaching impact on job creation in the construction sector (companies implementing the works), the industrial sector (companies producing the equipment and materials needed), and the service sector (companies monitoring quality of service, issuing various building certificates, marketing, and the like.) The EEO Scheme can help energize the BiH economy, which is why it is also viewed as a means of development. In addition, the implementation costs of the EEO Schemes are much lower because of the existing infrastructure of the obligated energy distributors and/or retail energy sales companies. The EEO Financial Architecture is shown in Figure 3.

In the implementation of energy efficiency measures, besides the part of the cost covered by the EEO mechanism (subsidy), interested beneficiaries pay for the remaining part of the total costs of the energy efficiency

**Figure 3. EEO Financial Architecture**

works on their building; the remaining funds can be financed fully from the beneficiaries' own funds or through other financing sources, such as a bank loan or an EE Fund. An example of a financial structure for the implementation of EE measures for a single beneficiary is shown in the Figure 4 below.

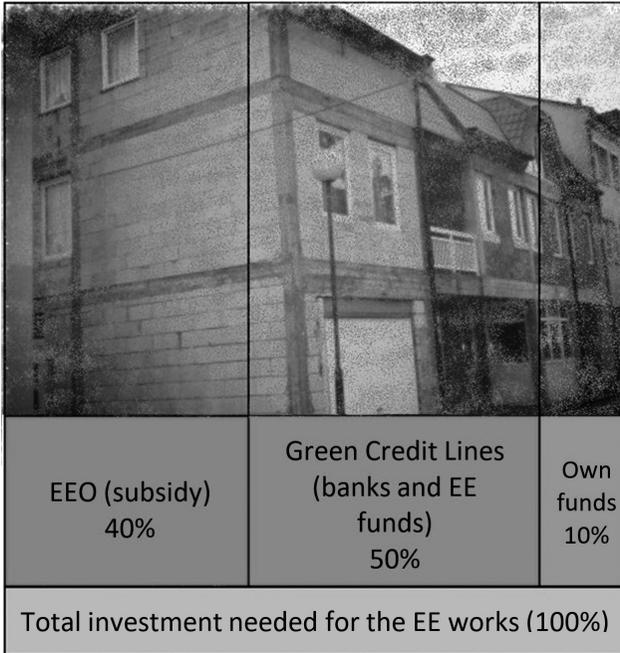
### Advantages of Investments in Energy Efficiency Measures through the EEO

Based on the market-based instruments for the IEA Energy Efficiency Report that analyzes 52 EEO mechanisms across the world, significant amounts of energy for less than the cost of supply are being saved through EEOs.<sup>10</sup> The blue columns in the table below show the expenditures by obligated parties per kWh saved in U.S. states and other countries. The variations in program costs are due to different factors, such as the amount of annual investment, policy focus, and overlap with other instruments if more than one market-based instrument is utilized.

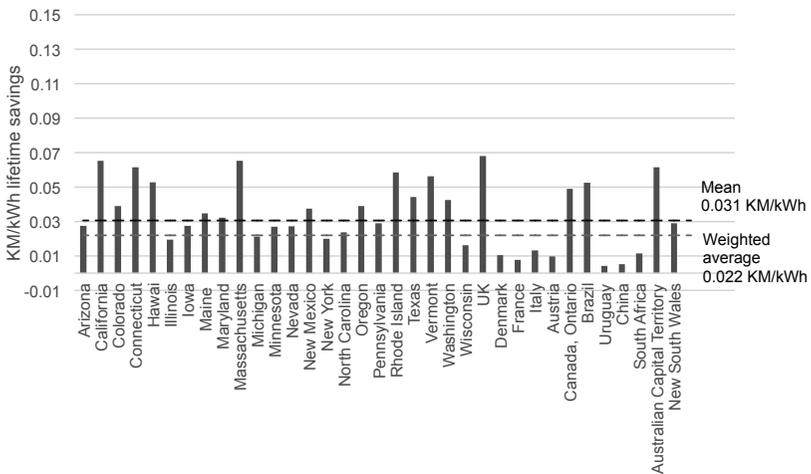
As explained by Figure 4, the total cost of the EE measures comprises the EEO subsidy portion plus the additional portion of the costs covered by the beneficiaries. Figure 5 above shows only the expenditures by the

<sup>10</sup> International Energy Agency, *op cit.*

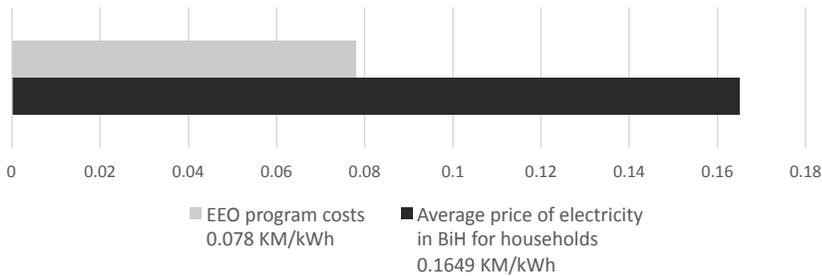
**Figure 4. Financial Structure for a Single Beneficiary**



**Figure 5. Expenditure by obligated parties per unit of energy saved**



**Figure 6. Total EEO Program Costs in Comparison with Electricity Price for Households in BiH, USAID EIA**



obligated parties that make up the EEO subsidy. If we assume that a leverage ratio of three is used, meaning that approximately 60 percent of the total funds needed are covered by the beneficiaries, while the remainder is provided by the obligated parties, then the total EEO program costs (EEO subsidy + beneficiary funds) would add up to 0.078 BAM/kWh lifetime savings.

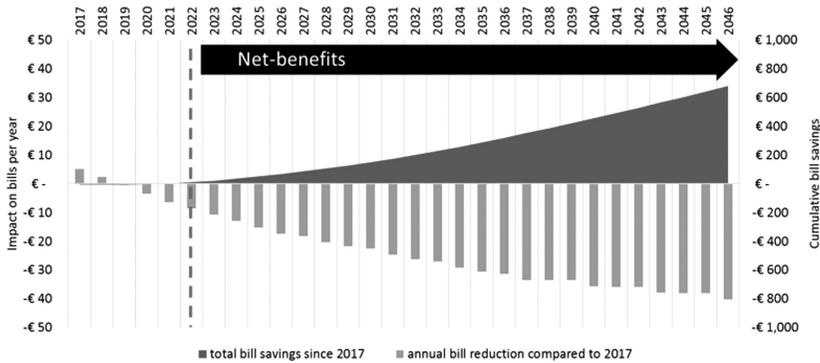
In comparison with the average cost of electricity for households in BiH, it is on average more than two times cheaper to invest in energy efficiency measures through the EEO and save energy rather than purchase the same amount of energy. The price for a kWh of electricity in BiH is about 0.1649 BAM/kWh for households, while the average cost of the saved energy based on the data from functioning EEO schemes across the world would be approximately 0.078 BAM/kWh lifetime savings as shown in Figure 6 above.

### Long-Term Impact on Energy Bills for Households

Figure 7 below shows the net benefits for household energy bills of an EEO mechanism that lasts for 30 years. Note that even though the average energy bill amount in the initial period increases, over the long run, the amount of average bills decreases significantly.

The size of the energy savings target determines the overall effectiveness of an EEO model. If the target size is too low, very little energy savings over what would be attained in any event will be delivered, and there is a risk that the obligated parties would simply be subsidizing those parties who would have installed energy efficiency measures even in the absence of the EEO scheme. If the target is too high, obligated parties will incur

**Figure 7. Potential Impact on Household Energy Bills for an EEO Lasting for 30 Years, USAID EIA**



higher costs, which will be passed on to consumers, and struggle to meet a target, which would undermine the credibility of the effectiveness of an EEO model.

The EEO model can and should be revised if the annual reports show that the effectiveness of the model can be improved.

## Transparency

Since the Energy Regulators have legal requirements to operate transparently, the fact that the EEO mechanisms are administered by the Energy Regulators means that the functioning of the mechanism and supervision of the obligated parties in the implementation of energy efficiency measures will be transparent. All steps in the selection of the beneficiaries will also be outlined in detail by the Energy Regulators, giving clear instructions to the Obligated Parties how the transparency of the process will be run, how the beneficiaries apply for EEO subsidies and what criteria is used for their selection.

In addition, web-based platforms run by the regulatory commissions that clearly outline the EEO process, the selection criteria and ranking-lists for selecting beneficiaries, reporting and monitoring processes also contribute to the transparency of the whole process.

## **Why Invest in Energy Efficiency Measures?**

Energy efficiency should not be viewed only as an obligation, but also as a development opportunity for the overall economy of the country. In the following sections of the paper, an annual investment of 100 million BAM into energy efficiency measures will be used as a reference point for estimates that underscore the benefits of investing in energy efficiency measures.

## **Significant Increase in Gross Domestic Product (GDP)**

In the economy, there is a circular flow of income and spending. Money that is earned flows from one entity to another, and most of it gets spent repeatedly as an investment or purchasing different goods and services, trickling down the value chain. This means that small increases in spending from consumers, businesses or the government lead to much larger increases in economic output. When money spent multiplies as it filters through the economy, economists call it the “multiplier effect.” According to studies done in the European Union, the GDP multiplier for energy efficiency measures is up to 3.7 times.<sup>11</sup> This means that for every BAM spent on EE measures, GDP increases by 3.7 BAM, as illustrated in Figure 8 below:

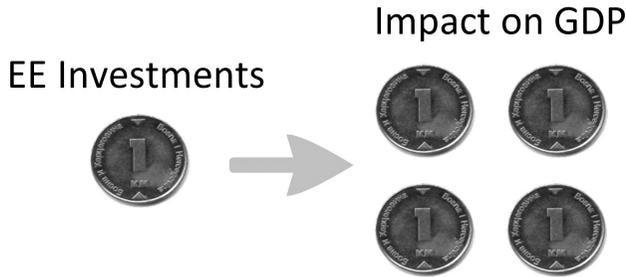
For an annual investment of 100 million BAM in energy efficiency measures, due to the mentioned multiplier effect, the annual increase in BiH’s GDP would be around 370 million BAM. For example, through an increase in GDP, other benefits such as increased revenues from taxes and social security contributions can be calculated. Based on the proportion of taxes (21.9 percent) and social security contributions (15.7 percent) of the BiH GDP,<sup>12</sup> this means that an increase of the BiH GDP by 370 million BAM would result in 81 million BAM in additional revenues from direct and indirect taxes and 58 million BAM in additional income from social security contributions.

---

<sup>11</sup> Change in GDP per unit of investment (EUR/EUR), table 2.4: <https://www.iea.org/publications/freepublications/publication/capturing-the-multiple-benefits-of-energy-efficiency.html>.

<sup>12</sup> IMF Country Report No. 16/291.

**Figure 8. Illustration Showing the GDP Multiplier of Energy Efficiency Investments**



### Decreasing the Energy Intensity of BiH

Energy intensity is a measure of the energy efficiency of a nation's economy. The energy intensity of a country indicates the quantity of energy required per unit of Gross Domestic Product (GDP): using less energy to produce the same quantity of GDP would lower the energy intensity of a country. Based on the energy intensity indicator shown below, BiH has the highest energy intensity in the region and is almost five times more inefficient than the EU-28 as shown in Figure 9 below. The lower the energy intensity, the more competitive a country is.

Energy efficiency is a proven way to reduce a country's energy intensity.

### New Jobs

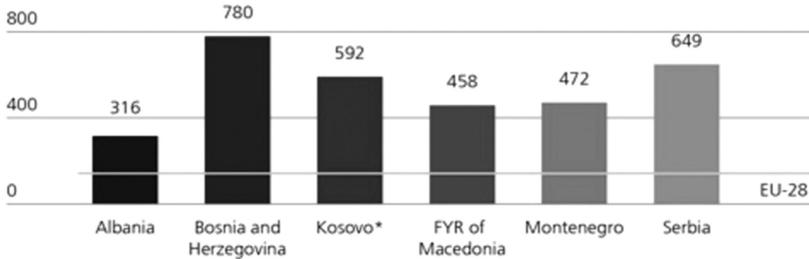
The investment of 100 million BAM in energy efficiency measures in BiH would result in the creation of nearly 4,900 direct full-time jobs. This data is calculated according to the Green Jobs Report,<sup>14</sup> which analyzed investments into energy efficiency measures for 34 facilities in BiH and its effects on direct employment.

The allotment and the type of works in the implementation of energy efficiency measures in buildings in BiH is shown in Figure 10 below. The

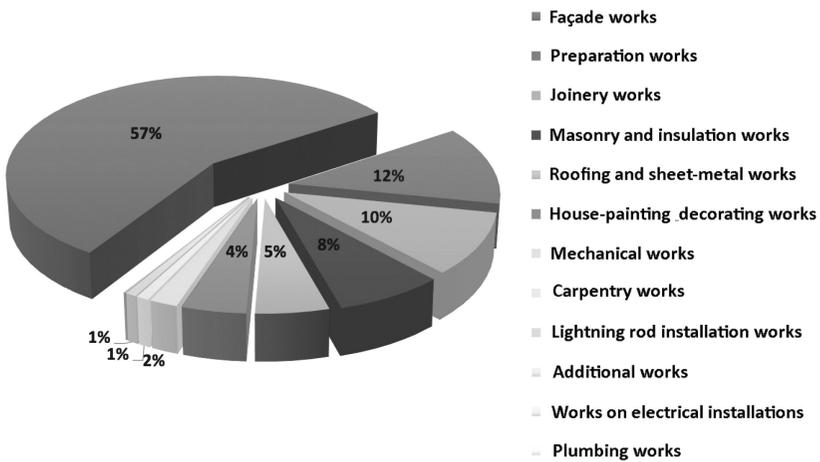
<sup>13</sup> [www.energy-community.org/portal/page/portal/ENC\\_HOME/ENERGY\\_COMMUNITY/Overview/Characterising](http://www.energy-community.org/portal/page/portal/ENC_HOME/ENERGY_COMMUNITY/Overview/Characterising).

<sup>14</sup> Green Jobs Analyzing the Employment Impact of Energy Efficiency Measures in Bosnia and Herzegovina, CRP, UNDP 2016.

**Figure 9. Energy Intensity of the Economy in 2013 [Gross Inland Energy Consumption (toe) / Gross Domestic Product (million EUR)]<sup>13</sup>**



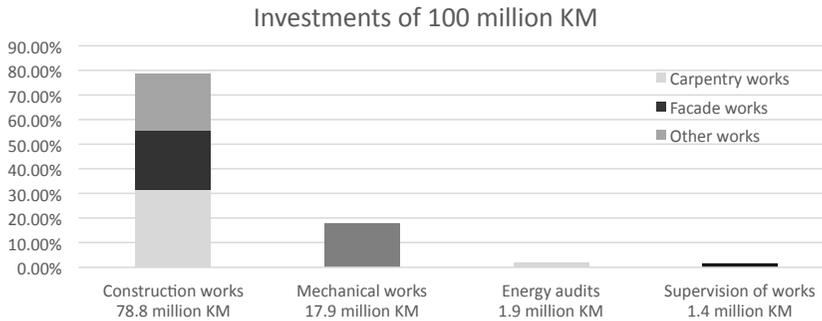
**Figure 10. Types of Works in Implemented EE Measures**



pie chart indicates which industries make up the biggest share of works and have the greatest potential for new employment.

### Engagement of Domestic Industries by Type of Energy Efficiency Works

Figure 11 below shows the allocation of funds invested into energy efficiency measures in buildings grouped by the type of work (the costs in Figure 11 include materials, equipment and labor costs). The proportions

**Figure 11. Allocation of Funds by the Type of Works**

shown in the Green Jobs Report have been scaled up for an investment of 100 million BAM annually.

Within the total investment of the 100 million BAM shown in the illustration above, the share of carpentry works is about 32 million BAM and facade works are about 24 million BAM. Table 2 below depicts these works in terms of square meters of installed facades and windows.

**Table 2. Approximate Quantities and Unit Prices for Carpentry and Façade Works Through EEO**

	Investment	Price (BAM per m <sup>2</sup> )	Quantity (m <sup>2</sup> )
Carpentry works	32 million BAM	188	170,000
Façade works	24 million BAM	40	600,000

Based on analysis of the current market for facades and windows, currently in BiH 1.8 million m<sup>2</sup> of facades and 123,000 m<sup>2</sup> of windows are sold annually for the residential sector.<sup>15</sup> The implementation of the EEO in the residential sector would more than double the demand for windows in BiH and increase the demand for facades by a third, thus allowing for additional jobs and revenues for SMEs active in these sectors.

<sup>15</sup> The quantities of sold EE products in BiH and their prices have been derived from market surveys as presented in the report, “Market Analysis of Distributed Products for Energy Efficiency in BiH,” Association of BiH Thermo-engineers, financed by the GIZ Promotion of Energy Efficiency in BiH Project.

## Energy Security

The International Energy Agency (IEA) defines energy security as the uninterrupted availability of energy sources at an affordable price. Energy security has many aspects: long-term energy security mainly deals with timely investments to supply energy in line with economic developments and environmental needs. On the other hand, short-term energy security focuses on the ability of the energy system to react promptly to sudden changes in the supply-demand balance.<sup>16</sup>

Energy efficiency can be considered as a local energy resource since any quantity of energy that is saved does not have to be purchased in the first place. This means that instead of building new power plants to cope with rising energy demand, the energy savings made through the implementation of energy efficiency measures can postpone the building of new power plants or make them entirely unnecessary. Investing in energy efficiency is the quickest and least costly way of addressing energy security both on the individual and countrywide level.

Through the annual investment of 100 million BAM into energy efficiency measures in buildings, approximately 64 GWh<sup>17</sup> of energy could be saved annually in BiH. These annual energy savings are equivalent to the annual electricity usage of some 17,000 average BiH households.

## Reduction of Air Pollution

An investment of 100 million BAM per year in energy efficiency measures in buildings would reduce CO<sub>2</sub> emissions by approximately 36,000 tons per year,<sup>18</sup> which is equivalent to the annual CO<sub>2</sub> emissions made by some 19,000 cars.

---

<sup>16</sup> <https://www.iea.org/topics/energysecurity/subtopics/whatisenergysecurity/>.

<sup>17</sup> The amount of the energy saved has been extrapolated from the results of the USAID 3E Project that implemented energy efficiency measures in BiH, as described in the report “Energy Efficiency in Public and Residential Sectors—Projects Development and Implementation,” USAID 3E, Spring 2014.

<sup>18</sup> The amount of the CO<sub>2</sub> reduction has been extrapolated from the results of the USAID 3E Project that implemented energy efficiency measures in BiH, *Ibid.*

## Conclusion

As explained in this paper, EEO schemes have proven to be excellent mechanisms to stimulate the economy of the countries that implement them. Through this instrument, energy efficiency measures are financed on a large scale through a domestic financing source that does not depend on donor funding or loans. This has far-reaching impact on job creation in the construction, industrial, and service sectors. Finally, the EEO mechanism can help energize the BiH economy, which is why it is viewed as a development mechanism.

What remains to be done next is the relevant BiH governments must reach a decision on which mechanism to implement, and then tackle the process of amending the necessary legislation.

## Annex

The EEO Working Group, composed of all relevant ministries and institutions, was formed in 2015 in Bosnia and Herzegovina. The EEO Working Group is working with the assistance of the USAID Energy Investment Activity on the development of the detailed design, documents and procedures so that the necessary legislation can be drafted for the implementation of the EEO. The required EEO formation steps have been addressed for BiH, with the implementing parties defined and necessary tasks required, as set forth below:

- EEO target-setting body: Government.
- EEO administering body: Energy Regulator.
- Obligated parties: Electricity Distribution Companies.
- Target size: Carry out an assessment of the current supply chain and increase the EEO target gradually over time commensurate with growth in the BiH supply chain. This will allow the local EE industry to develop and avoid the imports that would be required if local industry does not have the time to grow fast enough to meet the demand.
- Obligation period: Set the target over a ten-year period to provide stability and allow for sufficient flexibility to modify the EEO model as needed.
- Sectoral coverage: Focus on the residential sector, as this sector provides significant potential for replicable low-cost energy efficiency

measures and is a major contributor to energy demand in Bosnia and Herzegovina. In particular, the focus should be on vulnerable customers.

- **Fuel coverage:** Oblige only electricity companies initially but allow them to achieve their targets through energy savings across all fuels.
- **Eligible measures:** Use only standardized measures, as they reduce the administrative burden and keep the scheme manageable.
- **Reporting:** Establish clear reporting requirements for obligated parties.
- **Monitoring and verification:** Implement robust monitoring and verification requirements.
- **Compliance:** Put in place penalties that are significantly higher than the cost of delivering the target.



## *Chapter 12*

# **A Cashless Society is a Fairer Society: Reducing the Shadow Economy Through Financial Inclusion and the Promotion of Electronic Payments**

*Artur Turemka*

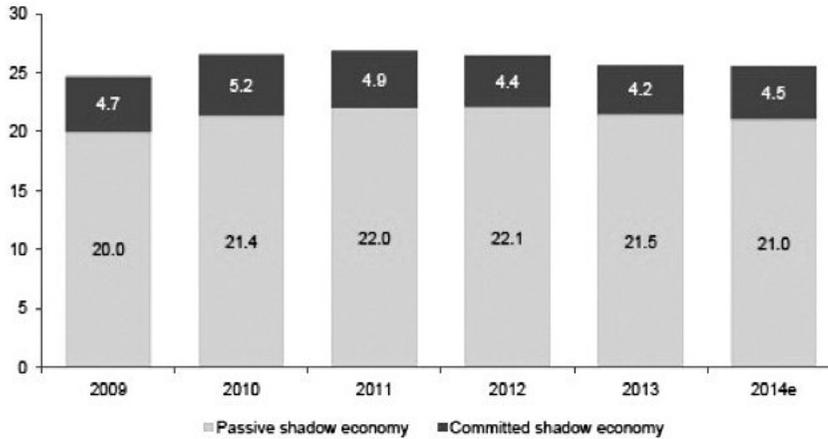
Each year, national governments in Europe lose billions of euros in tax revenue, directly impacting public investments in schools, healthcare, infrastructure, and other structural spending. The European Commission recently published the annual VAT Gap study,<sup>1</sup> indicating the situation has not improved in recent years and is showing an alarming trend. In 2014, over 160 billion euros in tax revenue was lost in the EU. This underscores that an effective tax collection system is paramount to improve a fairer tax collection for citizens and a greater VAT revenue for governments. EU and national governments are stepping up their efforts to clamp down on tax evasion. The same effort is observed in Bosnia and Herzegovina (BiH), a Balkan country on its way to EU accession.

Levels of shadow economy presence vary significantly across Europe, with a particularly high presence in Central and Eastern Europe. A recent EY study adopts an innovative approach to the measurement of the shadow economy, including its development over time, its structure, and sectorial breakdown. The study, commissioned by Mastercard, covers eight countries in Central and Southern Europe—Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Poland, Serbia, Slovakia, and Slovenia. The research also offers a contribution to the analysis of different regulatory measures to reduce the shadow economy through the promotion of electronic payments.

The EY study distinguishes between two categories of the shadow economy: a committed shadow economy, and a passive shadow economy. In the former, both sides of the transaction benefit from using cash, which enables them to evade tax liabilities and to sell and buy illegal products

---

<sup>1</sup> “VAT Gap: Nearly €160 billion lost in uncollected revenues in the EU in 2014.” European Commission . September 6, 2016. [http://europa.eu/rapid/press-release\\_IP-16-2936\\_en.htm](http://europa.eu/rapid/press-release_IP-16-2936_en.htm).

**Figure 1. Shadow economy in BiH as a percentage of GDP**

Notes: Shadow economy figures for 2014 are based on estimates/forecasts of some of the shadow economy determinants.  
Source: EY

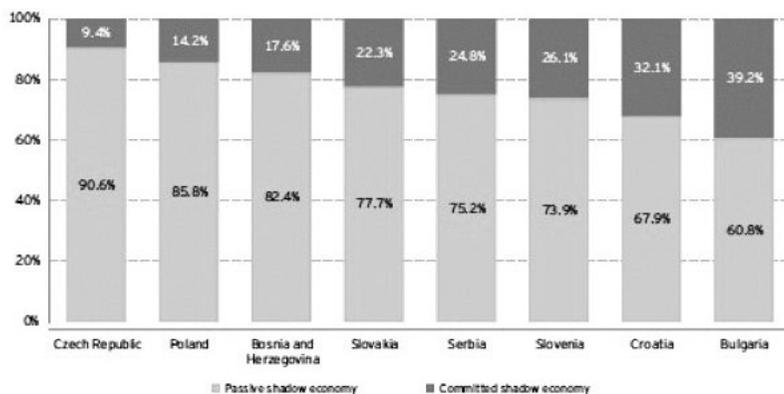
and services. In the latter, one party (the consumer) pays in cash while only the other party (the seller) reaps the benefits by hiding the income. Thus, consumers may not even be aware that they are contributing to the expansion of the shadow economy. In this particular case, cash payments provide an opportunity as well as an incentive not to report the transaction and evade tax payments by the seller.

According to the study, the passive shadow economy is estimated to stand between 9 percent and 25 percent of GDP in Central and Eastern European countries. The obtained results for Bosnia and Herzegovina show that from 2009 to 2011, at the peak time of the global financial crisis, BiH saw an increase in the level of the undeclared economy, which reached between 24.7 percent to 26.9 percent of GDP.<sup>2</sup> After its peak in 2011, the level of the shadow economy started to decline, and in 2014 it was estimated to amount to 25.5 percent of GDP. The food, beverage, and tobacco sector is estimated to be the most affected, with a 42 percent share of the total passive shadow economy in BiH. As the main component of the overall non-observed economy in Bosnia and Herzegovina, the passive shadow economy had an upward trend until 2012, and started to decline in the following year, to amount to 21 percent of GDP in 2014.<sup>3</sup>

<sup>2</sup> EY “Reducing the shadow economy through electronic payments. Bosnia and Herzegovina,” p. 7.

<sup>4</sup> Ibid.

**Figure 2. Structure of the shadow economy in 2014 across the analyzed countries**



Notes: Shadow economy figures for 2014 are based on the estimates/forecasts of some of the shadow economy determinants.  
Source: EY

For the eight countries analyzed, the passive component of shadow economy accounts for a vast majority (61 to 91 percent) of their unregistered economy. It entails some serious consequences, one of them being government losses in VAT and CIT revenues, which range from 1.6 percent of GDP (Slovenia) to 4.2 percent of GDP (Bosnia and Herzegovina).<sup>4</sup> In Bosnia and Herzegovina, the government's loss of revenues is approximately 1.1 billion BAM, or 4.2 percent of GDP.<sup>5</sup>

## Electronic Payments Shed Light on the Shadow

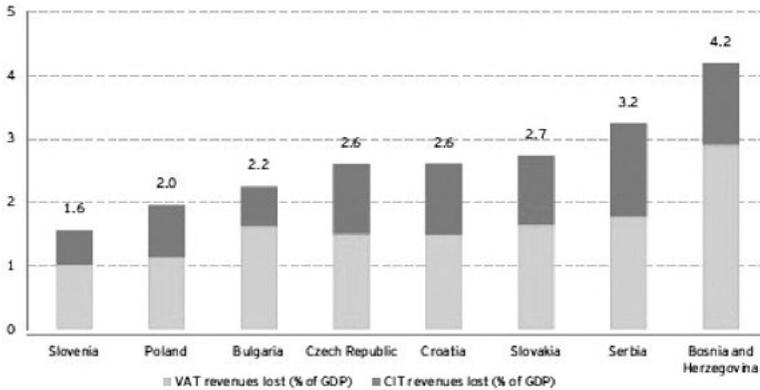
The inability to trace cash transactions translates into the avoidance of taxes and a larger presence of the shadow economy. For a country, this means lower budgetary funds, smaller investments in modernization of production processes, less funds for healthcare, education, and infrastructure—in short, a stalling economy. The solution? Moving away from cash, and encouraging electronic forms of payment.

Policymakers are increasingly aware of the benefits of curbing cash. Dutch MEP Cora Van Nieuwenhuizen recently said, “The number of financial transactions which are unknown to tax authorities has to decrease

<sup>4</sup> EY “Reducing the shadow economy through electronic payments. Bosnia and Herzegovina,” p. 31.

<sup>5</sup> *Ibid.*, p. 10.

**Figure 3. Lost government revenues due to the existence of a passive shadow economy in 2014**



Source: EY

drastically and there is a concrete way to make this happen: the facilitation and promotion of electronic payments. One of the many advantages of paying electronically is that it is traceable and there is proof of the transaction.”<sup>6</sup>

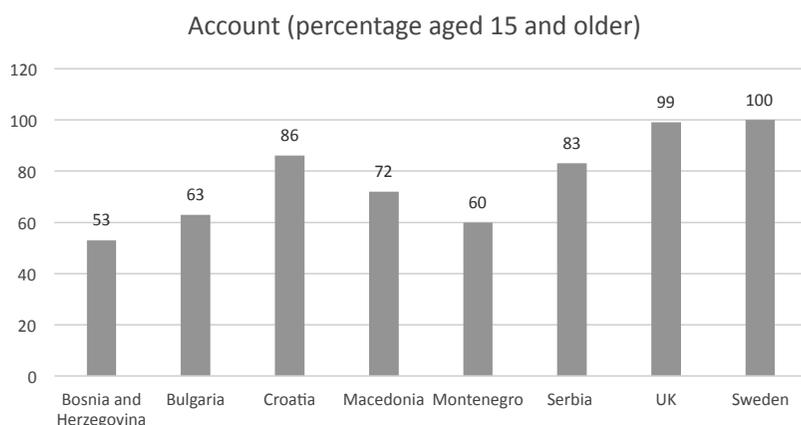
However, the shift from cash to electronic payments is slow. It is a fact that governments that took measures to facilitate the use of electronic payments have seen their tax revenue increase. According to EY, doubling the value of electronic payments should lead to a reduction of the shadow economy of up to 3.7 percent of GDP and an increase in government revenues of up to 0.8 percent of GDP. Moving to a cashless society is a gradual process that requires balanced policy measures which are a combination of incentives and obligations.

### Including the Financially Excluded

The very first step in creating a cashless society must be the inclusion of all those that are financially excluded, i.e., all those who do not have access to basic services we take for granted. According to the World Bank, the percentage of citizens with bank accounts is 52.7 percent in Bosnia and Herzegovina, coming in last in the region and seriously lagging behind developed countries, where the figure is nearly 100 percent. A large number

<sup>6</sup> Lane, Jason. "A cashless society is a fairer society." Euractiv. September 13, 2016. <https://www.euractiv.com/section/euro-finance/opinion/a-cashless-society-is-a-fairer-society/>.

**Figure 4**

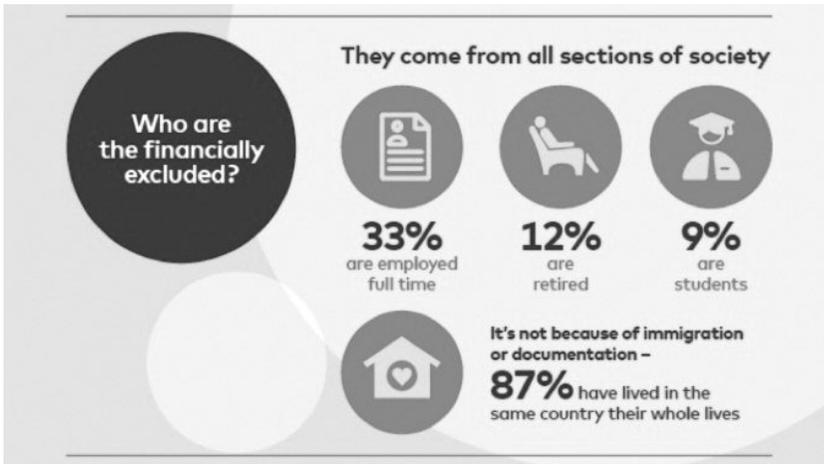


	2011	2014
Account at a financial institution (percentage aged 15 and older)	56.2	52.7
Account (percentage aged 15 and older)	56.2	52.7
Account at a financial institution, female (percentage aged 15 and older)	47.7	47.1
Account at a financial institution, male (percentage aged 15 and older)	67.2	58.8
Account at a financial institution, income, richest 60 percent (percentage aged 15 and older)	63.1	59.6
Account at a financial institution, income, poorest 40 percent (percentage aged 15 and older)	45.9	42.3
Account at a financial institution, older adults (percentage aged 25 and older)	58.1	56.1

Source: World Bank

of students are also underserved. Of young adults aged between 15–24 only 34.4 percent have an account.<sup>7</sup> Only 18.6 percent of adults aged 15+ use an account to receive wages, and a mere 2.1 percent use it for government transfers. There are instances where merchants are willing to give a small discount to customers if they pay in cash because it enables them to not pay a banking fee and not to report the transaction and consequently not pay the tax.

<sup>7</sup> "Financial Inclusion Data/Global Findex." World Bank. <http://datatopics.worldbank.org/financialinclusion/country/bosnia-and-herzegovina>.

**Figure 5**

Source: "The Road to Inclusion." Mastercard Financial Inclusion Survey. December 5, 2016. [https://newsroom.mastercard.com/wp-content/uploads/2016/12/Road-to-Inclusion\\_Mastercard-Financial-Inclusion-Survey-2016.pdf](https://newsroom.mastercard.com/wp-content/uploads/2016/12/Road-to-Inclusion_Mastercard-Financial-Inclusion-Survey-2016.pdf).

As these numbers clearly show, financial exclusion is not a problem isolated to the developing world. Some 138 million people across Europe still live outside the financial system, pay inflated costs to cash paychecks or borrow money to cover immediate needs. They live in urban centers, they are mothers, students and farmers.

According to a new research conducted by Mastercard, which comprised a face-to-face survey among 635 respondents in France, Italy, Poland, Russia, and the UK, a third (33 percent) of financially excluded people have full-time employment. The research highlighted some of the existing misconceptions around financial inclusion revealing that 87 percent of the financially excluded people surveyed have lived in the same country their whole lives.<sup>8</sup>

The World Bank regards technology as one of the main facilitators of financial inclusion. In the last three years, access to technology has increased

<sup>8</sup> Mastercard conducted a face-to-face survey among 635 respondents in 6 markets (UK, Poland, Italy, Russia, France and Spain) across Europe. Interviewing for these surveys took place between 18th July and 10th August 2016. The margin of error for this study is  $\pm 3.0$  percent at the total level, and  $\pm 6.0$  percent at the market level. The survey was administered by Ipsos, a global research and survey company.

### **Bosnia and Herzegovina Market Trends: Mastercard Perspective**

Bosnia and Herzegovina is a predominantly debit market, as debit cards make up for 83 percent of all products.

According to the official data of the Central bank, there has been a 4.5 percent increase in the number of cards issued in BiH. The total annual overturn per card has increased, while average transactions have slightly decreased. This clearly shows that people have recognized the value of cards for everyday use. And these transactions are safe, fast, and convenient.

Despite this positive trend, Bosnia and Herzegovina remains a cash heavy economy—90 percent of all transactions are in cash. Practicality, convenience and safety of payment are all advantages of electronic payments over cash, and these are key elements of our communication strategy. Cash creates costs for all parties involved—retailers, banks, consumers, and governments.

In the Balkan region, and in Bosnia and Herzegovina in particular, there is a serious need for greater education on the benefits of electronic payments, and the long term challenge is to correct the false perceptions of cash payments. Greater card acceptance could contribute to reducing the presence of a passive shadow economy and drive greater financial inclusion.

significantly (in 2013 it was 29 percent; in 2016, it was 49 percent). Yet, access to financial services is not growing at the same rate. Advances in technology create greater opportunities, but if access to it is not inclusive for all members of society, it can have the reverse effect on financial inclusion.

Every digital device has the potential to be a commercial device. But if we simply digitize the tools without extending them to those outside the system, we risk having the “Internet of Everything” without the “Inclusion of Everyone.”

The challenges to financial inclusion governments around the world are facing are similar.

- Ensure financial access and services extend to hard-to-reach populations;

- Increase citizens' financial literacy;
- Devise useful and relevant financial products, tailored to consumer needs;
- Drive best practice guidelines to ensure fees and pricing are clear and visible to the consumer—to encourage take up and usage and thus avoiding unexpected charges to leading to nervousness or continued cash usage/gray economy.

In partnership with financial institutions, merchants, telecommunications companies, governments, and non-governmental organizations (NGOs), Mastercard has been using its technology, scale and capacity to address inequalities. We have already helped make the financial system more accessible to hundreds of millions of people who were previously excluded through more than 1,000 government programs in more than 60 countries. We have committed to bringing 500 million people and 40 million small merchants and micro-entrepreneurs into the financial mainstream by 2020.

The lack of financial inclusion for so many, weakens the economic and social stability in Bosnia and Herzegovina. Access to basic financial tools creates economic opportunity and growth, individual empowerment and dignity, and can help reduce poverty. These tools provide greater opportunity for more people to lead self-determined lives. They give a world which is currently only operating at half capacity and harnessing only half the talent, an opportunity to operate closer to full capacity.

## **Development of Payment Infrastructure**

Another important step in the fight against shadow economy would be the development of a payment infrastructure.

Despite the positive trends observed in the Bosnian market, financial infrastructure is still underdeveloped. Both the number of cards and terminals in Bosnia and Herzegovina is the lowest in the region, while the value of card transactions (in GDP percentage) is one of the lowest among selected European countries. In 2014, in Bosnia and Herzegovina there were 5.474 POS terminals per 1,000 inhabitants.

By simply growing the acceptance infrastructure to 37 POS terminals per 1,000 inhabitants (the same penetration level as in Finland) in the sectors most affected by the shadow economy (food, beverage, and tobacco supply, the fuel sector and the hospitality industry), the effect of the

measure will contribute to the contraction of the passive shadow economy with -0.64 percent of GDP.<sup>9</sup> In government revenues, this translates into 35.5 million BAM per year. Therefore, changes in merchants' willingness to accept electronic payments, as well as improvement in the payment infrastructure are highly desirable.<sup>10</sup>

In an effort to support accessibility and modernize payment infrastructure in rural areas, the Romanian government adopted a bill that regulates cash-back at the point of sale and obliges merchants to install a terminal as of a certain turnover threshold.

### **Incentives for Consumers**

Introducing incentives for consumers to use electronic payments is estimated to have significantly positive effects on the presence of a shadow economy in Bosnia and Herzegovina.

Special benefits directly related to consumer payments cards provided by private financial institutions such as cash back, reward points or discounts have already proven to be effective method of incentivizing consumers to use their cards more often.

According to the EY study, similar incentives can be provided by the government through appropriately designed tax incentives that reduce the tax component of retail prices such as VAT, if the consumer decides to pay electronically for his/her purchase.<sup>11</sup>

A similar measure has been adopted recently in Bulgaria. The parliament adopted a tax relief for physical entities that receive 100 percent of their income via bank account and spend 80 percent of it via electronic form of payment.

Merchants and consumers however only represent one side of the story. Governments manage millions of payments every day such as taxes, invoices, etc. Promoting electronic payments for government acceptance and disbursements is therefore critical.

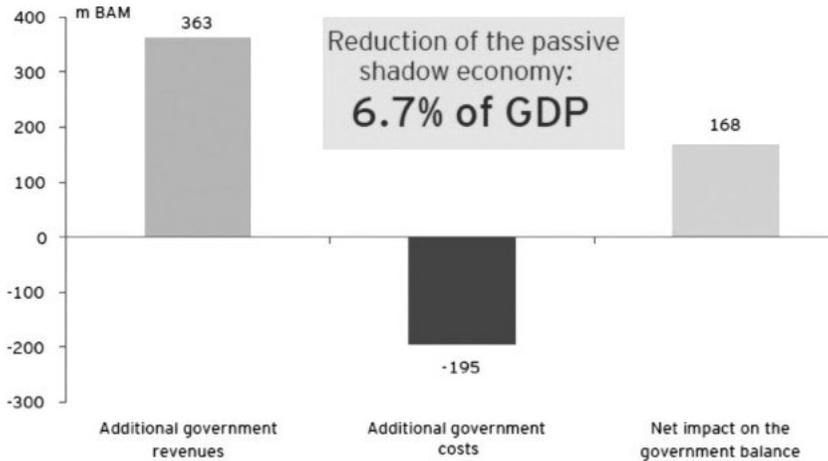
---

<sup>9</sup> EY "Reducing the shadow economy through electronic payments. Bosnia and Herzegovina," p. 25.

<sup>10</sup> *Ibid*, p. 13.

<sup>11</sup> *Ibid*, p. 27.

**Figure 6. The impact of the optimum cash-back for card payments (1.7 percent of card payment value) on government revenues in Bosnia and Herzegovina**



Source: EY

## Government Disbursements

Bosnia and Herzegovina spent over 12 percent of GDP on public sector wages in 2013, a substantially greater amount than countries such as Macedonia and Albania, which spent around 5 percent of GDP in the same year. Bosnia and Herzegovina's spending on non-contributory social assistance is by far the largest in the region and the largest in Emerging Europe at close to 4 percent of GDP.<sup>12</sup>

The introduction of electronic payments for social and health welfare disbursements to citizens has proven to be an effective method for reducing fraud, raising legitimate claim rates, and reducing process and administrative savings. In South Africa, the move of social welfare payments from cash to cards generated an estimated 320 million euros in cost savings by 2017, and the catching of 150,000 fraudulent applications.

In Italy, millions of citizens can now pay their taxes and utility bills faster and more easily because the government enabled the acceptance of electronic payments at nearly 70,000 new locations and more than 100,000 points of sale nationwide.

<sup>12</sup> IMF Country Report No. 15/299, October 15, 2015, p. 8.

## **Fiscal Receipt Lotteries**

Once the infrastructure is there, governments can change consumer and merchant behavior. Examples of this were the recent campaigns launched in Romania, Serbia, Bulgaria, and Croatia to leverage lotteries to drive card usage.

There are many other concrete examples that governments can follow to fight the shadow economy and build a more sustainable and transparent tax collection system. As illustrated above, the total payment value chain needs to be targeted and measures should range from strengthening payment infrastructures, encouraging merchant and government acceptance and incentivising consumer use. While the results of the European Commission's VAT Gap Study remind us how important the fight against tax evasion is, best practices in Europe show that policymakers can make a difference by adopting the right policy solutions.<sup>13</sup>

---

<sup>13</sup> For more reference on the EY study and its methodology: <http://www.ey.com/pl/pl/services/tax/vat—gst-and-other-sales-taxes/electronic-payments-en>; [http://www.ey.com/Publication/vwLUAssets/Shadow\\_Economy\\_-\\_Bosnia/\\$FILE/REPORT\\_ShadowEconomy\\_Bosnia\\_and\\_Herzegovina\\_17.pdf](http://www.ey.com/Publication/vwLUAssets/Shadow_Economy_-_Bosnia/$FILE/REPORT_ShadowEconomy_Bosnia_and_Herzegovina_17.pdf); [http://www.ey.com/Publication/vwLUAssets/Report\\_Shadow\\_Economy/\\$FILE/REPORT\\_ShadowEconomy\\_FINAL\\_17.pdf](http://www.ey.com/Publication/vwLUAssets/Report_Shadow_Economy/$FILE/REPORT_ShadowEconomy_FINAL_17.pdf); [http://www.ey.com/Publication/vwLUAssets/EY\\_Polska\\_-\\_Raport/\\$FILE/Technical\\_APPENDICES\\_17.pdf](http://www.ey.com/Publication/vwLUAssets/EY_Polska_-_Raport/$FILE/Technical_APPENDICES_17.pdf).



## Chapter 13

# Bringing Bosnia and Herzegovina to the Global Tourism Market: Reforms for a Better Future

*Dejan Radmilović*

As the world tourism market is recovering from the effects of the economic slowdown following the 2008–2009 recession, it is becoming clear the sector is well on its way to become an important global industry. In 2015, tourism amounted to 7 percent of the world's export in goods and services. In addition to receipts earned in destinations (amounting to 1.26 trillion dollars), international tourism also generated 211 billion dollars in exports through international passenger transport services rendered to non-residents in 2015, bringing the total value of tourism exports up to almost 1.5 trillion dollars, or an average of 4 billion dollars a day.<sup>1</sup>

This increase in tourism is the result of several factors, the most important being globalization as an inevitable process following developments in transportation and communication technologies. It is now easier than ever before to share and find information, and to travel around the world. However, tourist demand is differentiated according to the cultural diversity of attractive destinations. This results in the rejection of the concept of a “world culture,” which would in effect decrease the need and desire to visit authentic locations, and this rejection works well in favor of tourism growth.

Bosnia and Herzegovina has tremendous capacity for the growth and development of this sector due to its unique combination of natural resources and a rich cultural heritage. The sector could become a major driving force for the economy, allowing other industries in the country to grow and develop through the fresh capital pouring in. This would also allow for easier implementation of reforms and could contribute to the development of both the country as a whole, as well as local communities. However, even though BiH has increased in popularity as an attractive destination in recent years, with 776,889 international tourist arrivals in 2016 (an increase of 14.54 percent from 2015),<sup>2</sup> it is still nowhere near its

---

<sup>1</sup> UNWTO “*Tourism Highlights*,” 2016 Edition, 2016, pp. 2–3.

<sup>2</sup> Agency for Statistics of Bosnia And Herzegovina *Tourism Statistics: Cumulative data, January–December 2016*, 2017, p. 2.

maximum potential. Current developments in the tourism sector of Bosnia and Herzegovina are at a very low level and, for the most part, not coordinated and streamlined properly. To change the current state of affairs, a wholesome approach is needed, taking into account several factors, ranging from global tourism trends and the concepts of sustainable growth to local interaction and the legal framework.

## **An Overview of Tourism in Bosnia and Herzegovina**

Despite its huge potential, tourism in Bosnia and Herzegovina is only in the initial stages of development. In 2016, tourists in Bosnia and Herzegovina counted to 1,148,530 tourist arrivals which represent an increase of 11.6 percent and 2,376,743 overnight stays, or an increase of 10.9 percent as compared to the same period in 2015. The number of domestic tourist nights increased by 2.5 percent, and the number of foreign tourist overnight stays increased by 15.1 percent as compared to the same period in 2015. Domestic tourist's share of total number of overnight stays was 30.9 percent and foreign tourists share was 69.1 percent.<sup>3</sup>

Concerning the structure of foreign tourist nights, most of them (49 percent) were realized by tourists from Croatia (11.9 percent), Serbia (8.4 percent), Turkey (8.1 percent), Italy (6.5 percent), Slovenia (6.0 percent), Poland (4.1 percent) and Germany (4.0 percent). Tourists from other countries realized 51 percent of tourist overnight stays.<sup>4</sup>

Regarding the average detention of foreign tourist stays, Malta comes in first with an average stay of 5.5 nights, South Africa with 3.9 nights, Ireland with 3.5 nights and Lithuania and Kuwait by 3.4 nights each. According to the type of accommodation facility, the highest number of nights was recorded in hotels and similar accommodation with share of 92.4 percent.<sup>5</sup>

It is estimated that the tourism sector (defined here narrowly as businesses with direct activity in catering, hotels, and lodging) achieved receipts amounting to 656 million dollars in 2016,<sup>6</sup> accounting for 4.05 percent of the country's GDP (16.182 billion dollars),<sup>7</sup> and help employ over

<sup>3</sup> Agency for Statistics of Bosnia And Herzegovina *Tourism Statistics: Cumulative data, January–December 2016, 2017*, p. 2.

<sup>4</sup> Ibid.

<sup>5</sup> Ibid.

<sup>6</sup> UNWTO. "Tourism Highlights," 2016 Edition, 2016, p. 5.

<sup>7</sup> World Bank. "World Bank national accounts data, and OECD National Accounts data files," 2017.

35,000 workers in the accommodation and food service activities alone.<sup>8</sup> In addition, the tourism industry, including indirect effects on sectors related to tourism (transport, trade, banking, financial services, entertainment, construction, real estate, sports, culture, etc.) has a larger effect for the country. Considering the wider effects of tourism on the economy, and based on global trends, it is estimated that the tourism industry adds over 1.5 billion dollars, and affects over 90,000 jobs. Considering the presence of an extensive shadow economy, these figures could increase by up to 40 percent.<sup>9</sup> A more in-depth and focused study needs to be conducted to properly gauge the effects of the shadow economy on tourism, and to formulate action plans to reduce it.

The legal framework is, just like the administrative system in the country, quite complex, with laws being on the entity level.<sup>10</sup> In the Federation of Bosnia and Herzegovina (FBiH) this is even more pronounced, as cantons<sup>11</sup> also have their own laws regarding tourism and the environment.<sup>12</sup> This has proven to be a problem, as there have been several instances where laws on different levels of government in FBiH contradicted each other, negatively affecting the administrative and institutional approach to the development of tourism, and greatly slowing down its progress.<sup>13</sup>

On a more positive side, certain key objectives, such as the ones set out in the Strategy for the Development of the tourism sector in FBiH for 2008–18, are likely to be realized, based on current data and growth trends. The document set out to increase the number of tourists in 2018 to 924,000 with an annual growth rate of 4 percent and reach 3,262,000 overnight stays with a growth rate of 8 percent. Additionally, the Strategy anticipated

---

<sup>8</sup> Agency for Statistics of Bosnia And Herzegovina. “*Persons in paid employment by activity*,” December 2016.

<sup>9</sup> EY (Ernst & Young), “*Reducing the Shadow Economy through Electronic Payments: Bosnia and Herzegovina*,” 2016.

<sup>10</sup> Bosnia and Herzegovina has two entities, the Federation of Bosnia and Herzegovina (FBiH), and Republika Srpska (RS).

<sup>11</sup> FBiH consists of 10 cantons, which often have conflicting laws and administrative processes.

<sup>12</sup> See Federation of Bosnia and Herzegovina tourism related laws and bylaws: <http://www.fmoit.gov.ba/ba/page/23/zakonski-okvir#>; Republika Srpska tourism related laws and bylaws: <http://www.vladars.net/sr-SP-Cyrl/Vlada/Ministarstva/MTT/PAO/Akti/Pages/Zakonski-akti-u-oblastima-turizma-i-ugostiteljstva.aspx>; Canton Sarajevo tourism related laws and bylaws: [http://mp.ks.gov.ba/sites/mp.ks.gov.ba/files/zakon\\_o\\_turizmu\\_19\\_16.pdf](http://mp.ks.gov.ba/sites/mp.ks.gov.ba/files/zakon_o_turizmu_19_16.pdf)

<sup>13</sup> As was the case regarding the founding of the new Tourism association of Canton Sarajevo in 2016, where the legal status of the old association, supposedly founded on the Federal law was quite unclear

an increase in the direct contribution of tourism to GDP growth and employment, reaching 9.3 percent of GDP in 2018 (approx. 1.48 billion dollars) up from a 5.6 percent share in 2007. The total investment in the development of tourism is expected to reach about 1.6 billion dollars and other investments in the physical infrastructure should continue to open up new perspectives for tourism.<sup>14</sup> While the numbers seem highly optimistic, with increased support and investment in tourism, these objectives can be reached, and even surpassed.

### **Current Legislative and Institutional Framework Regarding Tourism in Bosnia and Herzegovina**

The institutional structure of BiH, which is often cited as one of the main obstacles to overall economic development, is also an obstacle to the development of tourism. Indeed, the institutional framework is complex, leaving little room for the efficiency and coordination of tourism activity in BiH. A simplified stratification of institutional infrastructure is shown in Tables 1 and 2 of competent institutions below.

However, slow progress in tourism development in BiH cannot be justified just with a complex institutional structure. Local authorities and local communities, as well as private business entities and tourist organizations, should be more active in facilitating the development of tourism within their jurisdiction and at the micro level.

Regarding legislation, there is no tourism law at the state level. According to the constitution of Bosnia and Herzegovina, tourism falls under the competencies of the entities and the Brčko District, while the state coordinates and coordinates existing laws. The legal regulation of tourism and accommodation in BiH is resolved with entity laws based on the following current laws: the law on tourism activity,<sup>15</sup> the law on accommodation<sup>16</sup> and tourism laws of the Brčko District.<sup>17</sup>

---

<sup>14</sup> Federal Ministry of Tourism and Environment, “*Strategy for development of tourism sector in FBiH for the period 2008–2018*,” 2008.

<sup>15</sup> FBiH: law on tourist activities (“Official Gazette of the Federation of BiH”, No. 32/09) RS: law on tourist activities (“Official Gazette of Republic of Srpska”, No. 45/17)

<sup>16</sup> FBiH: law on accommodation activities (“Official Gazette of the Federation of BiH”, No. 32/09) RS: Law On Accommodation Activities (“Official Gazette of Republic of Srpska”, No. 45/17)

<sup>17</sup> Brčko District: law on tourist activities of the Brčko District (“Official Gazette of the Brčko District”, No. 22/05)

**Table 1. Regulatory framework**

State level

<b>Institution</b>	<b>Role</b>
Ministry of Foreign Trade and Economic Relations of Bosnia and Herzegovina: Sector for natural resources, energy and environmental protection - Department of tourism	Coordination and the creation of tourism policies

Common body

<b>Institution</b>	<b>Role</b>
Work group for coordination of activities in tourism	<ul style="list-style-type: none"> <li>• Ensure that the tourism sector in BiH complies with the directives of the European Union and complies with the standards applicable in the EU countries,</li> <li>• Organize and regulate tourism in the tourism sector in accordance with legal regulations and to harmonize the level of joint activities, taking into account the existing legal framework, in order to contribute to the establishment of a single economic space in BiH, which is one of the key priorities of the European Partnership,</li> <li>• To establish an effective regulatory framework in the tourism sector in a way that strengthens the competencies of the existing institutions and establishes competencies of tourist associations in BiH,</li> <li>• Ensure efficient and coordinated work of the tourism structure of BiH</li> </ul>

Entity and BRCKO district level

<b>Institution</b>	<b>Role</b>
<ul style="list-style-type: none"> <li>• Federation of Bosnia and Herzegovina: Federal Ministry of Environment and Tourism – Sector for Tourism and Accommodation</li> <li>• Republika Srpska: Ministry of Trade and Tourism of the Republic of Srpska - Sector for Tourism and Accommodation</li> <li>• Brcko District: Department for Economic Development, Sports and Culture – Subdivision for Tourism</li> </ul>	Legislation and implementation of accompanying regulations

The working group consists of representatives from the Ministry of Foreign Trade and Economic Relations of BiH, representatives of entity ministries in charge of tourism, Brcko District representative and a representative of the Foreign Trade Chamber of BiH.

**Table 2. Institutional framework for support of promotion and strengthening of the tourism sector**

State level

<b>Institution</b>	<b>Role</b>
Foreign Trade Chamber of Bosnia and Herzegovina	Promotion, Strengthening of the Sector and Representing the Interest of Legal Persons in the Group for Tourism and Accommodation

Associations:

- Association of hoteliers and restaurateurs of BiH (UHIRBiH)
- Association of travel agencies of BiH (UTABiH)  
Strengthening the sector and advocating the interests of members of the association

Entity level

<b>Institution</b>	<b>Role</b>
Entity Chambers of Commerce:	Promotion, strengthening the sector and advocating the interests of legal entities in tourism and accommodation associations
• Chamber of Commerce of FBiH (Association of Trade and Tourism)	
• Chamber of Commerce of RS (Association for Tourism and Accommodation)	Promotion and strengthening of the tourism sector
Tourist boards and organizations:	
• Tourist Board of the FBiH • Tourist Board of the RS	

Canton level

<b>Institution</b>	<b>Role</b>
Cantonal Tourist Boards	Promotion and strengthening of the tourism sector in individual cantons

In the last year, there have been significant efforts in order to pass new laws on tourism and harmonize the entity laws on tourism with each other the EU *acquis* as much as possible. Republika Srpska has already passed a set of new laws regarding tourism,<sup>18</sup> while the Federation of Bosnia and Herzegovina has not yet passed any laws through the parliament, but are currently in the regular parliamentary procedure.<sup>19</sup> The laws of both entities are virtually identical, and the regulation of relations in the tourism

<sup>18</sup> Law on tourist activities (“Official Gazette of Republika Srpska”, No. 45/17); Law on accommodation activities (“Official Gazette of Republika Srpska”, No. 45/17)

<sup>19</sup> Draft law on tourism of the Federation of Bosnia and Herzegovina, number: 02-02-1826 / 16 of 26 September 2016; Draft law on residence taxes of the Federation of Bosnia and Herzegovina, No: 02-02-2255 / 16 of 12.12. In 2016

sector is based, *inter alia*, on the principles of comprehensive and sustainable development of tourism and related activities, harmonization of service levels in order to ensure uniform standards, protection of users of tourist services, the provision of a single, public electronic register of registered entities and data for the entity level, as well as on planning and implementation of tourism development policies in line with strategic documents.

Provided for in these laws, is the process of creating planning documents for this sector in both entities. These documents include a tourism development strategy, a tourism promotion plan, master plan, marketing plan, and a program for the development of tourism products. The tourism development strategy defines medium-term objectives for the planning and development of tourism for a minimum of five years adopted by the government at the suggestion of the competent ministry.

The tourism promotion plan includes research on target groups on the market, a specified marketing program, and other essential elements for tourism promotion. Companies and individuals participating in the tourism industry must be registered and must meet the requirements prescribed by the respective laws mentioned above. Tourist operators will have to ensure proper office space, facilities and equipment and meet the employee requirements. In addition, the laws help out fill the legal vacuum, defining tourist organizations in the entities, cantons, cities, and municipalities.

The laws contain a basis for establishing tourist organizations at the entity level, based in Sarajevo and Banja Luka, respectively. Their purpose is to create and promote tourism at the entity level. Also under its competence is the proposal and implementation of promotional activities in the entities and abroad, which are of common interest to all operators in the tourism industry and improve the complete tourist offer. They will also have to submit a financial report on operations for the previous year, to the entity governments no later than the deadline for adoption of the financial statements of the public institutions established by special regulations.

The governing bodies of the above-mentioned organizations consist of a supervisory board and a director, who is appointed by the entity governments. The Federal Ministry of Environment and Tourism and the RS Ministry of Trade and Tourism will establish and manage the electronic registry of tourism at the entity level. It will contain all registered tourist (travel) agencies, tour operators, and other organizations that provide tourist services.

The passing of this legislation is a start for the reform of the tourism sector, but their implementation is crucial. The sector can only thrive if the responsible agencies follow current global trends, and adjust their strategies, laws, and activities accordingly.

The Constitutional Court of the Federation of Bosnia and Herzegovina<sup>20</sup> declared the current federal Law on tourist organizations, the promotion of tourism, and all its bylaws unconstitutional, making the existing tourist board of Canton Sarajevo effectively non-existent. Nevertheless, the board remained operational, and even collected tourist taxes, but these funds were not diverted to the cantonal budget. This resulted in a dubious legal and factual situation, especially after a new law on tourism of Canton Sarajevo had been passed in April of 2016<sup>21</sup> and the government of Canton Sarajevo had established a “new” Sarajevo Canton tourist board.<sup>22</sup> Finally, in June 2017, the Cantonal administration for inspection issued a resolution<sup>23</sup> to close down the “old” Tourist Board of Canton Sarajevo because it did not have the necessary documentation to perform its work. This effectively means that Canton Sarajevo, one of main tourist centers in Bosnia and Herzegovina, will finally reach a greater level of transparency with a clear legal framework, thus allowing for an efficient use of the tourist tax-collected funds. These funds can then be reinvested to enhance the tourism sector in the canton, leading to a larger influx of tourists.

## Tourism and The Reform Agenda

Tourism is, by its nature, extremely sensitive to risk and uncertainty in the environment in which it operates and is constantly exposed to both external and internal shocks. For a well-functioning tourism sector, it is necessary to have a stable political situation and a secure environment, economic growth, and established transportation, infrastructure, and technology. The first three conditions are closely linked to the security and well-being of tourists, while the latter two enable the tourism industry to become a mass phenomenon. In all, tourism is very sensitive and uncertain when it comes to short-term and especially long-term planning.

---

<sup>20</sup> Constitutional Court of the Federation of Bosnia and Herzegovina—Ruling number: U-34-13 Date: 03.07.2014

<sup>21</sup> *Official Gazette of Canton Sarajevo* No. 19/16

<sup>22</sup> *Official Gazette of Canton Sarajevo* No. 38/16

<sup>23</sup> Cantonal administration for inspection issues—Resolution number: UP-1-14-08-20-09046/17 Date: 01.06.2017.

As political and economic instability are deeply interlinked with the well-functioning of the tourism sector, the success of the Reform Agenda of 2015–2018 will greatly impact the performance of this sector, as well as the international image of Bosnia and Herzegovina. The Reform Agenda itself is a product of necessity, being crucial in helping Bosnia and Herzegovina receive the EU candidacy status. The Council of Ministers of BiH, the government of the Federation of BiH, the government of Republika Srpska, and the governments of all ten cantons in the Federation of BiH and the Brčko District have started monetary recuperation procedures and the process of modernizing the economy to bolster a socially just and stable financial development. Additionally, the governments understand the critical need to increase job security, and to redesign social and welfare benefits.<sup>24</sup>

For example, guided by the objectives set out in the Reform Agenda, which foresees the abolition of parafiscal charges, membership fees are also abolished by the new set of tourism laws for RS and FBiH. Businesses in the FBiH, regardless of the activity they are engaged in, were obliged to pay 0.05 percent of the total annual turnover on behalf of the membership fee. In the future, this will be a great relief for all businesses, especially for those that do not have a direct connection with tourism. According to the Reform Agenda, business environment reforms will include simplifying and automating the registration of business entities, as well as obtaining various licenses, which will in turn lead to a greater number of private companies whose main activities are tied to tourism, and this will promote business growth and increase competitiveness in the field. This should result in a more diverse and numerous selection of tourist services, as well as improve quality and innovation in this sector.

## **Current Global Trends, opportunities for Bosnia And Herzegovina**

Current global trends in tourism (religious, adventure, eco-tourism, cultural, historical, and health tourism are gaining) present a great opportunity for Bosnia and Herzegovina. BiH certainly has potential to develop its tourism sector given its vast natural beauty and the uniqueness of its cultural heritage, but its lack of organized tourism at the national level

---

<sup>24</sup> Bosnia and Herzegovina: Council of Ministers of BiH, the government of the Federation of BiH, the government of Republika Srpska, the governments of the ten cantons in the Federation of BiH, and the government of the Brčko District. Reform Agenda 2015–2018.

and institutions at the state level (such as a National Tourism Organization, a National Tourism Agency, or a Ministry of Tourism), pose significant hurdles when it comes to the developing this sector and increasing global tourist flows. Tourism is a comparative (but not competitive) advantage of the BiH economy. In order to reach its maximum potential and increase competitiveness to a global scale, any development strategy must necessarily include tourism development at the national level and not merely at the entity and lower levels of government. Accordingly, it is necessary to provide an institutional framework at the national (state) level and form a NTO and NTA (Nationality Tourism Organization, Nationality Tourism Agency) to allow the structure of the sector to follow the organizational examples of leading tourist countries (e.g., Spain, France, Ireland, Greece, among others).

## **The Potential of Bosnia and Herzegovina**

Increasing competition in an ever-changing tourism market forces tourist organizations to keep upgrading and creating new offers. In an effort to attract more tourists and to increase the number of places visited, more tourist destinations around the world are boosting their efforts in marketing, with the aim of diversifying their portfolio. Bosnia and Herzegovina, having plenty of cultural and historical monuments, should be more creative in promoting its products. Moreover, tourism can constitute a mechanism of economic rejuvenation for the country and serve as a reason to increase efforts in preserving its cultural heritage. BiH offers a wide variety of types of tourism, with large potential to increase its visitors.

### ***Historical Tourism and UNESCO World Heritage sites***

Archaeological sites, cultural and historical monuments, cultural institutions, objects of religious architecture, are but a few segments of Bosnia and Herzegovina's cultural heritage, representing a unique mix of traditions, cultures, and religions that lived together for centuries, with strong Medieval, Byzantine, Ottoman, Austro-Hungarian, Central European influences.

Cities like Mostar, Počitelj, Banja Luka, Trebinje, Travnik, Bihać, Višegrad, Jajce, and others are engraved with memorials, monuments, and other signs of continued habitation from as early as the 1300s. Bosnia and Herzegovina is a meeting point for Judaism, Roman Catholicism, Christian Orthodoxy, and Islam with plenty of religious treasures for visitors.

Three important monuments and tourist attractions that are included at UNESCO World Heritage list are the Old Bridge in Mostar, Stehći in Herzegovina and the Mehmed Paša Sokolovic Bridge in Višegrad.<sup>25</sup>

### *Winter Tourism*

Bosnia and Herzegovina has a truly exquisite potential for mountain and ski tourism, as well as eco-tourism, spa tourism, and adventure tourism. BiH has a number of national parks, well-suited for eco-tourism.<sup>26</sup> Sutjeska national park is one of the first established in Europe and also includes Perućica, a thousand-year-old rainforest. BiH has two swamps that are home to bird habitats: Bardača (north) and Hutovo Blato (south). Both are declared “destinations of international significance” by the Ramsar International Convention.<sup>27</sup>

Sarajevo hosted the 1984 Winter Olympic Games, which, at the time, were the largest Winter Games ever (in terms of athletes and media).<sup>28</sup> Skiing, hiking, and alpinism tradition in Bosnia and Herzegovina has existed for over a hundred years, but the expansions of winter tourism came after the XIV Olympic Games held in 1984.

The canyons, lakes, clean rivers, waterfalls, springs, and many more unspoiled natural resources represents a unique eco-tourism offering. Furthermore, mountain villages offer tourists the possibility to enjoy the special rural ambient with traditional hospitality along with rich culinary offer of domestic products.

### *Health Tourism*

In recent years, the tourists are increasingly interested in spa tourism because the country is rich in high-quality thermal and mineral springs, health resorts, and spas. Usually nestled in beautiful surroundings with unspoiled nature and clean air, these health resorts offer true rest and

---

<sup>25</sup> Unesco World Heritage Sites List—<http://whc.unesco.org/en/statesparties/ba>.

<sup>26</sup> Examples are: Sutjeska, Kozara and Una national parks, and Hutovo Blato, Bardača, Blidinje nature parks.

<sup>27</sup> The Ramsar Convention on Wetlands of International Importance especially as Waterfowl Habitat is an international treaty for the conservation and sustainable use of wetlands. It is also known as the Convention on Wetlands. It is named after the city of Ramsar in Iran, where the Convention was signed in 1971.

<sup>28</sup> Official report published by the Organising Committee of the XIVth Winter Olympic Games 1984 at Sarajevo—Available for download at <https://www.olympic.org/Sarajevo-1984>

relaxation, in addition to health care. At present, there are 15 health spas registered in BiH.<sup>29</sup> In the last few years, BiH has actively worked in upgrading its spas. However, most spas are in need of investment to modernize existing facilities and programs.

### *Adventure Tourism*

Bosnia and Herzegovina is an emerging adventure-tourism destination, with excellent whitewater rafting on the Una and Neretva rivers. Adventure trips and packages offer different types of active holidays for tourists including: rafting, kayaking, walking the canyons of a series of crystal clear waters of the river Tara, Una, Neretva, Vrbas, climbing rocks, hiking, mountain-biking, paragliding and hang- gliding, skydiving, adventure driving off-road vehicles in a beautiful and magical ambience of the Olympic Mountains, Treskavica, Romanija, Prenj, Čvrstica, Zelengora, Velež, Vranica, Ozren, etc.

Adventure tourism is still not sufficiently explored, but thanks to the natural beauty of the mountains, rivers, canyons, and lakes, adventure tourism can become BiH's tourism brand. In 2009 Rafting World Championship was successfully organized in Bosnia and Herzegovina at the Vrbas and Tara rivers.<sup>30</sup> With 23 kilometers of the Adriatic coast and 240 sunny days every year, Bosnia and Herzegovina attracts tourists from all over the world. The town of Neum represents Bosnia and Herzegovina's Adriatic gateway and is the only coastal town in Bosnia and Herzegovina. It was first mentioned in year 533 (under the name Neunense), and developed as a maritime retreat in 1965. The Old Town of Neum is 2 km inland. Scuba-diving, parasailing, boating and jet skiing can be arranged in any of the major hotels. Guests are also offered very attractive tourist visits to Dubrovnik, Mostar, Medjugorje, Hutovo Blato, and Vjetrenica. The current accommodation in Neum cannot meet the needs of tourists during the season, which offers investors an excellent opportunity for upgrading and construction of new facilities.

Overall, the tourism sector in BiH has enormous potential for development, possessing all preconditions to play a significant role within the

---

<sup>29</sup> They are located in the areas of Olovo, Fojnica, Bjeljina, Bihać, Srebrenica, Gradačac, Sarajevo, Kiseljak, Laktaši, Bosanska Dubica, Sanski Most, Teslić, Prnjavor, Banja Luka, and Višegrad

<sup>30</sup> World Rafting Championship History—<http://www.internationalrafting.com/events-2/world-rafting-championship/>.

country economy. For this reason, the tourism development was consequently recognized as one of the top priorities of the overall national economic development policy.

## **Foreign Investment in the Tourism Sector**

Significant foreign investors are bypassing BiH, and are not willing to invest capital in the construction of infrastructure and facilities, partly because of insecurities they face while conducting business and partly because of the lack of privatization in tourism areas. The share of investment in tourism facilities, apart from various hotels, in total investments is negligible. By analyzing the potential and attractiveness of Bosnia and Herzegovina, there is also a low share of foreign investment in tourism in the total foreign direct investments.

Approaching the EU, total investments in tourism should be significantly increased. The increase in foreign investments can only be achieved by building a better international image of the country, reducing political risk, increasing efficiency, creating a more stable and prosperous economy, and adequate protection of the living and working environment. Tourism needs the help of governments, however looking at their current budgets, it is difficult that such assistance can be obtained, but should create space for local and foreign companies willing to invest in tourist facilities to attract foreign investment in the tourism sector para-fiscal and non-tax payments should be reduced or eliminated entirely, and there should be a proposal for the reduction of VAT in tourism.

In the last decade, foreign direct investment in tourism almost did not exist. Fighting shadow economy in the private sector, along with better regulation of public-private partnership and the better usage of EU and other multilateral funds, Bosnia and Herzegovina would increase FDI's in tourism, as such measures would encourage investments.

The development of the tourism industry and foreign investment is based on significant tourism potential and the fact that tourism is a promising industry.

At the same time limitations that affect the development and investment in this area are currently:

1. Lack of funds for the construction of tourist infrastructure
2. Absence of Tourism Strategy of BiH (national scope)

3. Poor roads and transport infrastructure
4. Insufficient promotion of BiH-tourism in foreign markets

The Foreign Investment Promotion Agency plan for tourism development in BiH includes:

1. Development proposals for suitable tourism regions, locations for investment, profile foreign and domestic investors. These regions are:
  - The 20 km of coastline with the town of Neum, with the aim of developing marine tourism;
  - The central (mountainous) part with the possibility of development of rural and winter tourism;
  - The plains (balanced regional development).
2. Reduction of administrative barriers and increase of the protection of private property in facility construction process.
3. Building and rebuilding of infrastructure to connect and use tourism facilities, implementation of infrastructure projects in transport and regional infrastructure connectivity.
4. The creation of additional incentives for the inflow of FDI and domestic capital investments. Investment projects with tourist amenities, in Bosnia and Herzegovina, relate to: winter tourism, building of ski slopes with artificial snow; Development of rural tourism offering healthy food; construction of a hotel complex and a modern port for the reception of tourist boats in the port of Neum.

Locations suitable for new investment are mountains Jahorina, Bje-lašnica, Igman, Kupres plain, Vlašić plateau, rivers Una, Vrbas, Neretva. According to the recommendations of the OECD, it is necessary to develop targeted strategies, with the goal of fiscal and financial incentives, in accordance with the model, scope, and structure of the investment, which is looking to attract in particular the local community, and the region. Tourism is a promising economic sector, and has been recognized as a strategic sector. There is obviously a need for a strategic approach to planning and encouraging foreign direct investment in the tourism of Bosnia and Herzegovina. In order to encourage foreign investment and help create a favorable investment climate, several laws have been adopted: “the law on foreign direct investment policy in BiH,” which seeks to define clear, transparent, stable policy and legal framework for the protection of

foreign investors, “law on customs policy,” “law on profit tax,” “law on concessions of Bosnia and Herzegovina,” “foreign exchange act,” etc.

## **Conclusion**

In the short term, BiH needs to draw up a strategy for tourism development at the national level, with the aim of transforming its comparative advantages into competitive advantages, with parallel processes of building an adequate image and branding BiH as a distinctive and attractive tourist destination, and this process should be an effort shared by all levels of the government in Bosnia and Herzegovina.

Building up on the current institutional foundations, and in order to mitigate the fact that there is no ministry of tourism or agency for tourism on the national level, a tourism expert council should be established instead. Its main objective would be to further enhance cooperation between the administration, academic, and private sector by establishing a bridge to diminish the skills gap in tourism and enhance employer awareness about the benefits of employee training. The expert council could be initiated by a specific ministry (e.g., on the state level, this could be the foreign trade and economic relations of Bosnia and Herzegovina, but the council can be established on any level of government) or other government bodies and involve a broad range of stakeholders, including chambers of commerce, tourism associations, vocational training institutions and universities. Its activities could include sector analysis (e.g., scope of the sector, economic trends, workforce demographics) and skills gap analysis, as well as developing, implementing and monitoring programs to bridge the skills gap in the tourism industry (e.g., by fostering co-operation between tourism firms and VET providers).

BiH can improve its position in the regional market by building higher quality tourism with innovative concepts. They should avoid standard development models (such as ski or coastal resorts and other tourism products). For example, the development of state-level tourist routes would help compensate for a limited number of natural or historical heritage sites. Also, it would be useful to institutionalize incentives for private-sector investment in infrastructure projects and improve the visibility of tourism infrastructure through promotional materials easily accessible online and in tourist centers. Policymakers could consider supporting private-sector investment in infrastructure either directly (through grants and capital stakes) or indirectly (through incentives). They should consider

increasing the budget allocated to transport and further develop a coherent strategy for the road network.

In order to maintain a marketing strategy for BiH, tourism should primarily be directed towards the European market. Europe is the number one tourist destination in the world. Europe had about 608 million arrivals in 2015, or 55 percent of global tourism, and about 451 million dollars in tourism revenues, accounting for 36 percent of all international tourism revenues.<sup>31</sup>

On a more concrete level, BiH must compete with a wide choice of tourist destinations in attracting passengers. Nearby destinations like Croatia, Serbia, Montenegro, Turkey, and Bulgaria all have a significant budget for attracting tourists. It must first position itself before it can create a competitive advantage in relation to those destinations. Marketing must be based on research and on the needs of customers or visitors, reflecting the products and experiences that have been developed on the basis of market trends. Marketing plans should be long-term strategies, with the foresight of trends, themes and emerging markets. The marketing concept must be well integrated, from the first point of contact to the visit and after-sales service after-sales effects and customer satisfaction. The assessment of the marketing approach should also be permanent, carried out through surveys and research of visitor perception, business results and needs, in order to provide the necessary data for adapting and changing the marketing strategy as needed.

---

<sup>31</sup> UNWTO “*Tourism Highlights*,” 2016 Edition, 2016, pp. 2-3.

## *Chapter 14*

# **The IT Sector and How to Improve the Legal Framework in Bosnia and Herzegovina**

*Armin Talić and Marko Šiniković*

BIT Alliance is the leading association of software companies in Bosnia and Herzegovina, comprised of the most prominent firms in the information technology sector. The members reached 40 million BAM worth of exports in 2015 alone, and are employing 700 highly qualified staff. There are currently an estimated 2,500 to 3,500 programmers in Bosnia and Herzegovina.

Occupational associations of IT companies, such as BIT Alliance, are a critical factor for the development of growing IT industries. In Croatia, there is the Association of Software Exporters CISEx and in Serbia, the ICT Cluster in Vojvodina. In Bulgaria, several organizations are engaged in specific activities contributing to the development of the IT industry. Some of them were founded as early as 2001.

The development of the software industry in Bosnia and Herzegovina did not result from strategic measures of governmental institutions, as is the case in Romania and Bulgaria. The IT sector in BiH, and primarily the software industry, developed as a consequence of private sector IT start-ups, with contributions from the international diaspora. Even though this sector has lacked institutional support, the aggregate of IT companies has succeeded to develop a respectable industrial branch.

IT companies are typically divided into hardware firms and companies involved in software. Bosnia and Herzegovina has not yet developed the production of hardware components. Existing companies, even though employing large numbers, are mainly engaged in the distribution of their products. There are two groups of software developers: those who develop and create their own software solutions, and those who are in outsourcing, commissioned by successful international companies to develop software applications. BIT Alliance members are both developers of software and companies who provide programming services for foreign companies (outsourcing), which is currently the most promising segment of IT activities.

### **Projection of economic benefits from software industry development in Bosnia and Herzegovina**

According to a preliminary analysis of BIT Alliance, the annual income per software engineer ranges between 80,000 and 120,000 BAM. For example, the training of 1,000 new software engineers Bosnia and Herzegovina could generate—primarily from exports—more than 90 million BAM per year. With 12,000 software engineers, the BiH software industry could generate over one billion BAM of revenue and nearly equate its revenue with the strongest economic sector in BiH, the wood industry. For the sake of comparison, in the city of Timisoara (Romania), whose population size is similar to Sarajevo's (BiH), 7,000 software experts are trained every year through the Romanian educational system. By 2020, there will be about 300,000 IT experts in Romania. A shortage of software engineers in the world today amounts to 2 million and it is further increasing.

**1 software engineer = 90,000 BAM annual revenue**

**12,000 software engineers x 90,000 BAM = 1,080,000,000 BAM annually (one billion and 80 million BAM)**

**25,000 software engineers x 90,000 BAM = 2,250,000 BAM annually (2 billion and 250 million BAM)**

Bosnia and Herzegovina has the potential to train 25,000 software engineers. Thus, the software industry in Bosnia and Herzegovina, with an annual revenue of 2,250,000 BAM, would become the most powerful BiH industry and a driving engine for the country's economic development.

This chapter aims to offer strategic solutions for crucial shortcomings, challenges, and problems in the development of the software industry in BiH. This can be summarized as follows:

- A lack of trained IT staff and a lack of IT education;
- Underdeveloped IT infrastructure and lack of support for its development and;
- An unfavorable business and legislative environment.

## **Current State of Affairs**

### ***Shortage of IT staff***

Despite the fact that existing BiH companies have almost limitless possibilities for opening new work places in terms of administrative costs and support, their long-term existence is uncertain due to an insufficient number of trained professionals. Even now, they often find themselves rejecting exceptionally lucrative business opportunities due to labor limitations. Hence, the country directly loses millions of BAM on an annual basis. Bosnia and Herzegovina shares the destiny of other countries in the region, who suffer from an increasingly pronounced trend of IT brain-drain.

However, the problem in Bosnia and Herzegovina is even more noticeable given the weaknesses of its educational infrastructure relative to the educational systems in neighboring countries who “produce” a larger number of IT professionals. In addition, there is a lack of practical work training for IT professionals in order to keep up with developments and exceptionally fast development of new technologies. This appears to be the largest problem for the software industry in Bosnia and Herzegovina. Not only can this prevent further growth, but it can also make the entire sector stagnate, or even backtrack. Replacements for trained staff cannot be found in the current domestic or regional labor markets. Skilled labor has to be “trained.” The weak infrastructure and an unfavorable legal framework have a direct and indirect effect on the shortage of domestic IT staff.

### ***Weak IT Infrastructure and a Lack of Support for its Development***

Bosnia and Herzegovina is positioned at the very bottom of the list when it comes to investments in research and development. As a whole, BiH spends a mere 0.04 percent of GDP on the IT sector, while the world average is 2.7 percent. Yet, software companies contribute significantly to the country’s GDP, annually allocating up to 10 percent of revenue for research and development of new products and services in addition to investing ample resources for the training and education of their employees. Nevertheless, Sarajevo, Banja Luka, and Mostar only have one technological park each.

In contrast, Germany had 32 technological parks back in 1992. As a result of planned development, Berlin alone has 10,000 IT companies generating an income that exceeds 26 billion BAM, almost equal to the overall GDP of Bosnia and Herzegovina. The German IT industry

employs over 100,000 people. Ljubljana and Zagreb also have highly developed technological parks, founded in the early 1990s. Today, the Technological Park in Ljubljana comprises over 300 companies with more than 1,500 employees, mainly in the IT sector.

There are no state funds set aside for the development of the IT sector. Previously, IT companies could not apply for development funds. The lack of support by domestic companies is evident (mainly with majority state ownership) by means of using domestic software solutions. On the other hand, examples of successful long standing cooperation can be found in relations between economy and IT sector, for example in financial services sector. In this sector, domestic IT companies design and implement specialized products. Until today a significant progress has not been made in introduction of e-service in public sector in BiH, hence domestic IT sector had no opportunity for its own development in this way.

### *Unfavorable Legislative Framework and Business Conditions*

Government institutions and the wider public lack a general understanding of the IT sector. As a result, strategic support for the IT and software industry is lacking. This is particularly true compared to developed countries, but also relative to BiH's neighbors. Hence, BiH is lagging behind in terms of institutional support for the IT sector. Earlier government initiatives (policies, strategies and action plans for the development of the information society in BiH 2004–2010), even though outdated and inadequately implemented, have made progress in public awareness, but not in the context of support for the development of the software industry. In addition to lacking strategic documents, and most likely as a result of this, the country failed to adopt laws and regulations, establish an independent authorized institution, or implement financial measures. In short, the software industry has not been recognized as a strategic branch for the economy. The little public information available to attract foreign investment is outdated and provides erroneous guidelines to potential investors. It is encouraging that a new strategic document at the BiH level (Policy of information society development in BiH, Ministry of Communications and Transport BiH), even though not adopted, recognizes the software industry as a separate and important segment of the IT sector.

In a rapidly changing environment of technological development and market adjustment, the development of the software industry requires a concrete institutional approach. Strategic support for the software industry in other countries of the region have placed it ahead of BiH. For example,

concerning export of information technologies services in the context of overall export, Bosnia and Herzegovina is ranked 77<sup>th</sup> in the world, while Romania takes 18<sup>th</sup> place, Macedonia 37<sup>th</sup>, Bulgaria 41<sup>th</sup>, Montenegro 45<sup>th</sup>, and Croatia 50<sup>th</sup> place. Except in terms of internet usage, BiH is rated below all its neighboring countries. Bosnia and Herzegovina is falling behind mostly in the quality of IT education and training, as well as the lack of institutional support.

Similar trends are recorded in neighboring countries, with the exception of Romania (where the software industry takes third place of industries with the largest exports), has managed to advance its software industry to the most promising sector and the best business promoter for its country.

### **Advantages and Potential of the Software Industry, Examples in Other Countries**

The software industry contributes significantly to the overall GDP in BiH. Even though the industry cannot be compared to other branches of the economy in terms of overall exports, most notably with the wood processing industry which records exports exceeding one billion BAM, it does offer significant advantages for the BiH economy and its citizens. Software companies provide high class working conditions, salaries that are often 50 percent higher than the average BiH salary, ecologically clean products, the industry with the fastest growing exports, limited imports, high revenues, limited initial investment and ease of opening up shop. It is also significant in terms of its role in reducing brain-drain and the fact that new work places in this industry do not undermine development and business operations of smaller firms, which is often the case in other industry branches.

In addition to the numerical advantages over other industries, IT companies and their software solutions are a critical leverage for the development of other industries. According to research results, small and medium size enterprises (SMEs) who use innovative technologies, increase their revenue by up to 15 percent faster and open new work places almost twice as fast compared to their competitors. Also, the value of software industry is reflected in the fact that 60–70 percent of its labor in BiH constitutes of young people under the age of 35.

The software industry in BiH, though not very large, is advanced and competitive on the world market for outsourcing). IT engineers in BiH

often have years of experience in the world's leading software corporations, so in terms of their knowledge, skills, experience and insights into modern trends, they are frequently ahead of their colleagues in other European countries. This is important to note, because the revenue growth from BiH software companies has ranged between 200 percent to as high as 1,400 percent, and new employees have been added by a rate of almost 600 percent.

In neighboring Serbia, software exports exceeded the exports of traditional products such as raspberries and corn, contributing more than 580 million euros in 2015. In Croatia, 1 percent of the overall labor force, or an estimated 12,000 employees, works in software production.

### **Course of Action**

BIT Alliance has implemented a number of projects aimed as a response to the above-mentioned challenges of BiH's software industry. Among other things, a six-month professional education program "BIT Camp" was organized. As a result, 50 new programmers who completed their training received employment offers in BIT member companies. The "BIT Camp" has showed that intensive educational programs can effectively re-train people from diverse backgrounds such as political scientists, economists, or lawyers into IT specialists employable by the IT industry.

However, the high cost of education and training and the lack of subsidies and support halted the further implementation of this project. In order to have systematic solutions, the software sector needs participation of state institutions with a comprehensive and strategic approach.

BIT Alliance stresses the need for the software industry to have a separate development strategy, or to become a separate part of a strategic document for IT development at the national level due to specificities of its development, and in line with good practices of countries in the world and the region. A more specific approach on the national level would positively affect the IT sector's development at lower levels of government.

Even though the BiH Ministry for Communication and Transport is primarily responsible for the promotion and strategic development of the IT sector, it is necessary to involve other institutions as well, primarily the Ministry of Foreign Trade and Economic Relations, and the BiH Ministry of Foreign Affairs. Best practices from other countries in the region show a strong engagement of state agencies for the promotion of

their IT sectors.

After adopting a strategic document, all levels of government should adopt specified action plans. Such plans should specify support for start-ups, IT clusters, the setting up of IT parks, introducing tax reliefs and financial incentives for companies investing in research and development, subsidies for participation costs in foreign markets and fairs, improvement of the legislative framework, and most importantly, the improvement of education in the widest sense: revision of elementary and secondary school, and university curricula to better meet the needs of the IT industry, increase the number of students at technical faculties, re-training programs for the unemployed, improvement of scholarship policies, continued education and training of IT teaching staff according to the latest technological developments and changes in the market. It is also necessary to enhance development of informal education, spreading of informal IT education, online IT education and professional advancement.

The European Union is planning to invest almost 50 billion euros for the development of its digital infrastructure in the next four years. This could be an opportunity for Bosnia and Herzegovina as well.

Within this initiative, BIT Alliance does not merely identify problems and propose adequate solutions, but also offers cooperation with governmental institutions at all levels of government. It wishes to provide concrete contributions in implementing all plans and activities envisaged by future policies, strategies and action plans for the development of Bosnia and Herzegovina's software industry.

## **Appendix: A BiH IT Success Story**

A success story in Bosnia and Herzegovina's IT sector is Lanaco, the largest private system integrator and one of the most successful family IT companies in the Western Balkans, based in Banja Luka. The company was founded in 1990 in Banja Luka by Nebojša Ninić, who applied years of experience from his work in companies of the former Yugoslavia, including Rade Končar, Incel, Čajavec, and Medicinska Elektronika.

Today, Lanaco's business operations consist of 10 departments with more than 280 employees. These young, highly educated specialists are on average 28 years old and own more than 1,000 vendor certifications. Lanaco customers come from a wide range of sectors, including health-

care, education, tourism and hospitality, media, construction, manufacturing, retail, NGOs, and government institutions.

Part of Lanaco's market success lies in the fact that 80 percent of the company's revenue comes from its own products and services. Due to the healthy business model, the company is in position to annually invest 3.2 million euros in software development and more than 1 million euros in the education and training of its employees. These investments provide Lanaco with competitiveness on the regional market and create conditions for sustainable growth.

Aside from establishing a healthy financial plan, the company pays much attention to corporate social responsibility. Lanaco dedicates most of its efforts to projects involving students, in both in secondary schools and in universities. The latest education project introduces programming in secondary schools, and is named *Kamp mladih programera* "Pitam DA" (*Programmers' Youth Camp "I'm asking, YES"*).

Last December, the company opened its new headquarters with work space for 500 employees. The Lanaco Technology Center includes two facilities with a total space of 10,000m<sup>2</sup>, and is the biggest of its kind in Bosnia and Herzegovina. The heart of Lanaco Technology Center is its Tier 4 Data Center, which is part of Cisco Intercloud. Technology Center is also home of the biggest multi-vendor IT conference in Bosnia and Herzegovina, *Tech Hosted by LANACO*. This three-day conference has a regional multi-vendor matrix concept and is aims to connect global IT leaders with different segments of the public, including students.

Lanaco has received many vendor awards, most recently the Microsoft Country Partner 2016 in Toronto during the Microsoft Worldwide Partner Conference (now called *Microsoft Inspire*). Apart from this award, the company also received SAP silver and bronze awards for two consequent years, in 2016 and 2017, for the Central Eastern Europe in Business Transformation category. The Company's achievements in education were recognized by the Cambridge University publication in 2015 titled "Inspiring leadership and innovation," and in the 2014 edition titled "The Guide to Excellence."<sup>1</sup> In addition, Lanaco has been recognized by the public in Bosnia and Herzegovina as one of most sought-after employers, and has received several

---

<sup>1</sup> "LANACO in the Publication of the University of Cambridge." Lanaco. June 16, 2017. <https://www.lanaco.com/eng/News/Pages/LANACO-in-the-Publication-of-the-University-of-Cambridge.aspx>.

acknowledgements by Posao.ba, the leading job portal in the country, as the best employer<sup>2</sup> in Bosnia and Herzegovina's ICT sector.

Since April 2016, Lanaco is participating in the London Stock Exchange ELITE Program, yet another international confirmation of the company's business strategy validity, but also an opportunity to further develop its existing management approach, all the while having in mind the forthcoming requests of digital transformation on the global market.

---

<sup>2</sup> "LANACO most desirable employer in the ICT sector this year." Lanaco. April 28, 2017. <https://www.lanaco.com/eng/News/Pages/LANACO-most-desirable-employer-in-the-ICT-sector-this-year.aspx>.



## About the Authors

**Selma Osmanagić Agović** is an expert for capacity building and local governance at the United Nations Development Program in Bosnia and Herzegovina. For the last 10 years, Agović has been actively involved in projects and programs related to institution building, state management, European integration, local governance, anticorruption, and civil society development. She has held many presentations at different regional and international conferences and roundtables. Having worked for years on different projects establishing various institutional and legal reforms in Bosnia and Herzegovina, she gained significant experience in political and institutional set up of the Bosnia and Herzegovina and countries in the region. Agović has expertise working with institutional representatives from all administrative levels and expertise in designing capacity building activities for institutional representatives in order to assist them in improving their capacities for implementing different reforms. She has significant expertise in policy development, conducting research, legal analysis, developing policy papers, and policy studies, performing project evaluations, and evaluation of project proposals. She developed numerous policy papers as author and co-author for different national and regional think tanks and consultancy companies. Agović holds a Bachelor degree in Law and the Master degree in State Management and Humanitarian affairs from La Sapienza University in Rome, Italy.

**Adis Arapović** is political scientist, civic society activist, analyst, and critic of public policies and politics. He is a Ph.D. candidate in the area of theory of political parties and has authored two books, over 30 scientific papers and numerous analysis and studies. He is lecturer at the School of Political Studies of the Council of Europe in Bosnia and Herzegovina and political academies of political parties and international organizations. Arapović is currently the Program Manager in the Centers of Civic Initiatives (CCI), one of the most influential civic society organizations in Bosnia and Herzegovina. He graduated from the Faculty of Political Science at the University of Sarajevo, and holds Master of Science degree in the field of international relations and contemporary diplomacy.

**Adisa Omerbegović Arapović** is an Associate Professor at the International Burch University in Sarajevo. She is also the Vice Rector for Education at the International Burch University. Her academic research and teaching background is primarily in the area of macroeconomics but her research interests are also in the area of political economy and transition. Currently, she is a member of the Economic Council of the Government of the Federation of Bosnia and Herzegovina. She was the Dean of the Faculty of Economics at the Sarajevo School of Science and Technology. She holds an MBA and Ph.D. in International Finance and Macroeconomics from University Malaya, Malaysia.

**Ajka Baručić** is a project expert at the non-governmental organization Institute for Youth Development KULT in Sarajevo, and is currently working on the implementation of an initiative concerning employment and labor market “BH Business Site,” funded by the United States Agency for International Development (USAID). Over the past four years, she was an assistant at the Faculty of Economics of the University of Tuzla, for courses in entrepreneurship, SME Management, and Project Management. From 2014 to 2015 she worked as an Advisor to the Prime Minister for Economic Issues of the Tuzla Canton Government. While working at the Entrepreneurship Development Center, she also prepared the annual report of the Global Entrepreneurship Monitor for Bosnia and Herzegovina, as the world’s foremost academic study of entrepreneurship. Baručić holds a M.Sc. in Management, and has conducted research on the topic “Entrepreneurial education as a factor in recognizing entrepreneurial opportunities for launching a new business.” She completed her B.A. at the Faculty of Economics of the University of Tuzla with the highest honors. In the World Bank’s essay competition on the topic “Tackling Youth Unemployment in Bosnia and Herzegovina: My Generation’s View,” her essay was voted best of 150 submissions. She has authored numerous expert and scientific papers, and her research interests are mainly focused on employment, youth employment, the labor market, entrepreneurship, youth entrepreneurship, and the business environment.

**Srđan Blagovčanin** is a specialist in the field of rule of law, good governance and anti-corruption reforms, policies and legislation with more than 12 years of experience as manager, analyst and legal expert. Currently, he is Chairman of the Board of Directors of Transparency International Bosnia and Herzegovina (BiH). He has authored a number of studies and analyses on these topics, published by The Center for Transatlantic Relations at The Johns Hopkins University, Paul H. Nitze School of Advanced International Studies, (SAIS), the Friedrich Ebert Stiftung, Transparency

International, among others. He has worked with Transparency International, the World Bank, USAID, Global Integrity, and many other international and national organizations and institutions. He holds a LL.M. degree from the Karl-Franzes University, Graz, Austria, and a specialization in Law and Human Rights from the Washington College of Law, American University, Washington D.C. His field of interests is primarily the rule of law, public policy, anti-corruption, governance, state and institution building, and democratization.

**Tea Ivanović** is a Fellow at the Center for Transatlantic Relations at the Johns Hopkins University Paul H. Nitze School of Advanced International Studies (SAIS). She is also the Washington correspondent for Sarajevo-based *Oslobodjenje*. Previously, Ivanović was at the financial consultancy Capstone LLC, and at the Institute of International Finance (IIF), in Washington D.C. While completing her M.A., she was a Graduate Research Fellow at the Center for Constitutional Studies and Democratic Development (CCSDD) in Bologna, Italy. At SAIS Europe, she was involved with the organization of the 60th anniversary celebration of the SAIS Europe Center, and was the Vice-President and co-founder of the Women in International Affairs (WIA) organization. Ivanović has also worked at the United Nations University Institute of Comparative Integration Studies (UNU-CRIS) in Bruges, Belgium, where she was the editor for United Nations University publications, and organized a joint UNU-CRIS and International Studies Association (ISA) conference in Bruges. Ivanović published her undergraduate thesis “External Pressures and Domestic Changes: The European Union, Council of Europe, and the Minorities in Vojvodina” in the academic journal publication *Philologia*, which she presented at various conferences, including at the International Symposium on Cultural Diplomacy in the EU, in July 2013. She is the co-editor of *Iraqi Kurdistan Region: A Path Forward* (Brookings Institute/CTR, 2017). Ivanović wrote for the SAIS Johns Hopkins newspaper, the *SAIS Observer*, as a graduate student, and has contributed and co-authored articles for the *Huffington Post* and the *Cipher Brief*. She holds a M.A. in International Relations and International Economics from The Johns Hopkins Paul H. Nitze School of Advanced International Studies (SAIS), and graduated *Summa Cum Laude* and *Phi Beta Kappa* from her B.A. in International Studies from Virginia Tech, where she received a four-year athletic scholarship for the Division 1 varsity tennis team. She speaks English, Dutch, Serbo-Croatian, is conversational in French, and basic Italian.

**Mak Kamenica** is the Deputy Chief of Party of the USAID Energy Investment Activity (USAID EIA) in Bosnia and Herzegovina. Kamenica is also the Executive Director of the America-Bosnia Foundation since 2010. Prior to this Kamenica was the Deputy Chief of Party of the USAID Enterprise Energy Efficiency (USAID 3E) project, in Bosnia and Herzegovina. The USAID 3E project assisted BiH to promote energy efficiency technologies by developing demonstration projects in public and private buildings in BiH. Through this project, the capacities of the municipal public sector counterparts and small and medium-sized enterprises (SMEs) that implemented the works were increased, and public awareness about the benefits of energy efficiency was increased. He was a Fulbright Visiting Scholar at the New York Institute of Technology, department of Energy Management, doing research on energy efficiency and renewable energy topics. In addition, during his time in New York, Kamenica was an Advisor/Intern at the Mission of Bosnia and Herzegovina to the United Nations in New York and monitored the Second Committee of the UN General Assembly on issues that concern energy efficiency, climate change, environment and sustainability. Kamenica holds a Master of Science (M.Sc.) degree in Electrical Power Engineering from the Faculty of Electrical Engineering - University of Sarajevo, a certificate in Business Project Management from the School of Continuing and Professional Studies - New York University.

**Edin Karabeg** is the CEO of Sberbank BH, and is a member of the Sberbank Europe Group. He started his career in the OSCE as a Personal Officer. In 2003, he joined Bank Austria Creditanstalt AG (Unicredit Group) as an International Risk Manager, and was later seconded to HVB Splitska banka, in Croatia. From 2006, he served as Equity analyst in CAIB (Unicredit Markets and Investment banking). In August 2007, he was promoted to the Business Manager for Fixed Income, Currencies and Commodities in Unicredit Markets and Investment banking. He continued his career in Capital Bank (Hypo Investment Bank AG) in Macedonia as CEO and CRO. In 2010, he moved to Hypo Alpe Adria International as Head of Steering Non-Core Subsidiaries and as Managing Director in Hypo Alpe Adria Leasing Holding and Hypo Alpe Adria Leasing Macedonia. He was a member and Chairman of various subsidies of Hypo Alpe Adria International. Karabeg graduated in Business Administration and holds an MBA from the IMADEC University Vienna, in cooperation with The Red McCombs School of Business, Austin, Texas.

**Emir Klarić** has worked in various roles at the FBiH Institute for pension and disability insurance as a controller, head of department for charge of contributions, head of department for control, and most recently as a Chief internal auditor. He is a member of the BiH Association of internal auditors, as its first-generation graduate. Klarić has engaged with several projects implemented by the non-profit organisation Green Council, most recently with the Feasibility Study for a project on the production of thermal insulation materials made from sheep wool (2016). He graduated in economics from the Department of Business Economy at the University of Sarajevo.

**Sanela Klarić** is the Vice Rector of International Relations and Scientific Cooperation at the Department of Architecture, the Faculty of Engineering and Information Technologies, at the International Burch University in Sarajevo. Klarić is currently involved with the establishment of international projects, cooperation and joint scientific research, and the designing of effective training materials, including the exchange of best practices aimed at enabling students to comprehend the essence of the topic and sustainable development needs. She is the team leader for the project “Bio-Based Student Pavilion,” a learning-by-doing project that includes interdisciplinary approach to practical building by using natural, local, renewable and recycled materials, and building elements. Klarić is also the President of the non-profit association Green Council where she manages several different projects, such as the “Sustainable Agriculture in the Function of Sustainable Development” project, which aims to map the development of the agro-environment stakeholders in BiH (organic producers, renewable energy resources used at farms, institutions, certification bodies, media, CSOs, business, chambers of commerce, regional development agencies who are active in sustainable agriculture) and “Energy Efficiency in Buildings as a Basis for Achieving Sustainable Socio-Economic Growth in Bosnia and Herzegovina” (aimed at developing guidelines for future activities in the sector which will support sustainable local economy and investments in innovative clean technologies). She has more than 18 years of experience in architecture projects, designing and supervising residential and public building and interior design. She delivered a number of presentations at conferences, workshops, lectures on sustainable architecture, natural sustainable materials and green cities, and development and delivery of teaching methods and models that will cover sustainability and nature. Klarić has 18 years of experience in working with international organisations, as an independent consultant on capacity building, administration, finance and procurement management, program and project

development, and policy and research management. She is a member of the Steering Committee of the BiH Association of Architects, “Socialdemokrati IGG,” and the Organizational Committee of the Green Design Biennale and has participated in various conferences in BiH and the region. She is the co-author of a number of the scientific studies, publications, guidelines, and is the author of the book *Sustainable Housing*. Klarić is also a member of Executive Board for Association of Architects in BiH.

**Jelka Milićević** is the Deputy Prime Minister and Minister of Finance of the Federation of Bosnia and Herzegovina since 2015. From 1984 until now, she performed several important duties and was active in the private sector prior to joining the government. She was a researcher and project leader in the Soko Aviation Industry d.d. Mostar, Head of Accounting and Finance at JAS d.o.o. Mostar, associate of the Expert Team for Privatization of the Government of FBiH, Director of Soko Financije d.o.o. Mostar, Director of Internal Audit in Croatian Post d.d. Mostar, member of the Management Board of the Banking Agency of FBiH and president of the Audit Committee in “Aluminij” d.d. Mostar, Director of the Audit Company Rekonzult d.o.o. Between 1996 and 2011, she received several certificates. Milićević became a certified auditor and accountant, and received a certificate of consulting excellence (by USAID). She is an expert in banks and financial institutions. She graduated from the Faculty of Economics in Mostar.

**Darko Milunović** is an economist, currently a senior assistant in statistical analysis at the Faculty of Economics of the University of Banja Luka. He holds a Ph.D. from the Faculty of Economics in Belgrade, a Master of Statistics also from Faculty of Economics in Belgrade, and a B.A in economics from the University of Banja Luka. Previously, he was a senior assistant in medical statistical analysis at the Faculty of Medicine of the University of Banja Luka. He was also an analyst for statistical and market research at Business Advisor d.o.o Banja Luka, and director of ECO Group d.o.o Banja Luka. Milunović participated in numerous projects as a team member and project coordinator. He specializes in statistical analysis, and has participated in a number of socio-economic studies and analyses. In addition, he has significant experience in developing various projects in the field of ecology, energy efficiency and renewable energy.

**Goran Miraščić** currently holds a post at the World Bank, at the Office in Sarajevo, Bosnia and Herzegovina. Prior to this post, he served as an economic policy advisor to the Prime Minister of the Federation of Bosnia

and Herzegovina. Miraščić is an Assistant Professor of Economics at the University Sarajevo, at the School of Science and Technology. Since May 2011, he has been a member of an expert body of the Fiscal Council of Bosnia and Herzegovina and as of April 2017, a member of the Economic Council of Federation of Bosnia and Herzegovina. Miraščić has published many articles in the field of international economics, public sector economics, and public finance. He has participated in numerous domestic and international conferences. In January 2010, he earned a Ph.D. in Economics from the Faculty of Economics at the University of Tuzla, in Bosnia and Herzegovina. He received his B.A. and MBA degrees from Lindenwood University, St. Charles, Missouri.

**Adnan Muminović** serves as a Political Economic Advisor to the EU Special Representative in BiH. Prior to the EUSR, he interned at the German Bundestag in Berlin and Heinrich Boell Foundation in Washington D.C., and worked as a Political Advisor at the Norwegian Embassy in Sarajevo. Muminović currently also works as a Teaching Assistant at the School of Economics and Business in Sarajevo, where he teaches macroeconomics. He holds a B.A. in Economics from the School of Economic and Business in Sarajevo and an M.A. in European Studies from the Center for Interdisciplinary Studies of the University of Sarajevo.

**Heidi Obermeyer** is the Program Coordinator and a Fellow at the Center for Transatlantic Relations. Prior to joining the Center, she worked for the Department of State at the U.S. Embassy in Berlin, for the U.S. Commercial Service in Munich, and most recently in federal consulting in the Department of Veterans Affairs. She holds an M.A. in Political Science with a concentration in European Governance from the University of North Carolina at Chapel Hill where she wrote her thesis on the potential for radicalization among Somali migrants in the United Kingdom by Al-Shabaab. Obermeyer holds a B.A. in International Affairs, Germanic Studies, and Anthropology from the University of Colorado at Boulder. She completed coursework at Ludwig-Maximilians-Universität in Munich, Humboldt Universität and Freie Universität in Berlin, and at the University of Bath, England. She speaks German and some French, Spanish, and Russian.

**Gary O'Callaghan** serves as a Special Advisor to the EU Special Representative in BiH. O'Callaghan worked for the International Monetary Fund in 1990-2003 and helped prepare the membership application and first financing program for Bosnia and Herzegovina (BiH) in 1995. He was an Advisor to the first High Representative in BiH in 1996-1997 and

was the IMF's Resident Representative in Croatia in 1997-2001. He has also served as a Senior Advisor to the Prime Minister of Montenegro and was Dean of the Business School at Dubrovnik International University before taking his current position in early 2014. A native of Ireland, he divides his time between Dubrovnik and Ireland (when he is not in Sarajevo). He earned a Ph.D. in Economics from George Mason University, and holds a Master of Economics and a Bachelor's degree from University College Cork.

**Sean Parramore** is finishing his Ph.D. at Queen Mary University of London and is a member and advisor at the America-Bosnia Foundation working on mobilizing support for the socio-economic reforms program launched by the Center for Transatlantic Relations. A graduate of the Johns Hopkins University SAIS (BO'09/DC'10), he is based in Brussels, and works in Paris, London, and Washington, D.C. Sean's PhD investigates the drivers of real estate sector reforms that appear to enable business and reduce corruption risk in the Western Balkans. He has conducted extensive fieldwork in Bosnia and Herzegovina and Kosovo on the role of domestic and international actors—particularly the EU, the World Bank and USAID—in enabling transparent large-scale land acquisitions, addressing illegal construction and reducing land information asymmetries. His academic interests include land governance, corruption prevention, state-building and European integration. Sean is currently an associate lecturer teaching international political economy at the University of London Institute in Paris, and an Adam Smith fellow at the Mercatus Center, George Mason University. Before graduating from SAIS Sean studied international relations and law in Groningen, the Netherlands. He has published in journals and newspapers on Western Balkan affairs, including the Dutch national daily *NRC Handelsblad*. He was employed as a EU enlargement/foreign policy analyst in Brussels, where he worked for the European Commission, the European Stability Initiative, the President of the European Parliament and a MEP. He was in Belgrade and Sarajevo with the Konrad Adenauer Foundation's Southeast Europe Rule of Law program. He also worked on the UK Foreign and Commonwealth Office Bosnia-Herzegovina Fellowship Program and taught international relations in London.

**Dejan Radmilović** has been actively involved in the non-government sector in Bosnia and Herzegovina for several years, serving as a secretary and project manager for several associations, including the Federation of Bosnia and Herzegovina where he was involved with the initiative "Hori-

zon 2024,” supporting the economic and social development of BiH and the region. He has organized events and conferences dealing with these issues. He has particularly focused on the problem of depopulation in Bosnia and Herzegovina, and he organized a conference on the socioeconomic position of BiH. He was also the lead organizer of the international conference for investment and economic development in BiH and the region, held in Sarajevo in December 2015. He has worked on projects regarding the concept of “safe communities” as a necessary prerequisite for stability and development. In 2016, as a project manager and chairman of the supervisory board of the America-Bosnia Foundation, he was involved in several high-profile projects with the goal of helping support the implementation of the Reform Agenda for Bosnia and Herzegovina, which gathered key stakeholders, and helped take crucial steps forward. His video compilation, aimed at promoting the rich cultural heritage of Bosnia and Herzegovina titled *Walk Through the Centuries of Bosnia and Herzegovina*, shown at the 4th Annual Transatlantic Economic Forum at SAIS Johns Hopkins University in Washington D.C. in December 2016. He is currently engaged in the overall coordination of the process of European integration with the Office for European Integration in the FBiH government, works on multiple other projects and research activities. He received his B.A. and M.A. degrees in Law from the Faculty of Law of the University of Sarajevo.

**Marko Šiniković** is a Public Relations manager at Lanaco. He graduated in public relations and communications from the University of Banja Luka in 2014. He has experience working with electronic media: radio stations, TV stations, internet portals, social, and print media. Šiniković has also been a professional PR manager at various festivals, city events, and public campaigns.

**Armin Talić** is the General Manager at Bit Alliance, the leading association of software industry companies in Bosnia and Herzegovina. He is also Chairman of Organizing Committee of the CEO Conference at the Faculty of Economics of the University of Sarajevo, where he oversees 215 organizations, 121 speakers, 25 sponsors, 30 companies, 20 faculties, 20 non-governmental organizations, and 120 media agencies. He has extensive experience in project management and human resources, having organized over a dozen conferences at various universities in the Western Balkans. He is also an e-learning specialist for clients ranging from the Central Bank of Bosnia and Herzegovina, several UNDP programs, BH Telecom, to name a few. He is also an IT consultant and web developer

on an ad hoc basis, and has worked with several startups. Previously, he was an IT assistant at Prizma, a microcredit agency. Talić has written and contributed to several publications. He graduated with the highest honors from his B.A. in economics from the University of Sarajevo, and hold an M.A. in economics from the University of Sarajevo.

**Sasha Toperich** is a Senior Fellow and Mediterranean Basin Initiative Director at the Center for Transatlantic Relations (CTR), at the Paul H. Nitze School of Advanced International Studies (SAIS) of the Johns Hopkins University in Washington D.C. He is also the President of the America—Bosnia Foundation (ABF), President of the World Youth Leadership Network (WYLN), a business consultant to a number of companies worldwide, and a world-renowned pianist. Toperich is the co-chairman of the Mediterranean Women in Leadership and Civil Society Conference, and the chairman of the Supervisory Board at the Mediterranean Development Initiative in Tunisia, established as part of the Initiative. He is co-editor of the book *A New Paradigm: Perspectives on the Changing Mediterranean* (Brookings Institute/CTR, 2014) with Andrew Mullins, and *Challenges of Democracy in the European Union and Its Neighbors* (Brookings Institute/CTR, 2016) with Aylin Ünver Noi. He is the co-author of two papers in the book *Unfinished Business: Western Balkans and the International Community* (Brookings Institute/CTR, 2012), titled “The Regulatory Environment in the Financial System in Bosnia and Herzegovina and How to Improve It” and “A New Paradigm for the Mediterranean: US–North Africa–Southeast Europe.” He also co-authored the article “Challenges of Democracy in Bosnia-Herzegovina” in the book *Challenges of Democracy in the European Union and Its Neighbors* (Brookings Institute/CTR 2016). Toperich held several diplomatic positions for Bosnia and Herzegovina. In 2002-2003, he was an advisor to the Ambassador of Bosnia and Herzegovina to the United Nations, from 2003-2007, he was a Special Envoy of the Presidency of Bosnia and Herzegovina to the United States; and in 2009 and 2010, he served as a Counselor at the Permanent Mission of Bosnia and Herzegovina to the United Nations. He is a featured columnist at U.S.Military.com, holds a blog at the *Huffington Post*, and is a contributor to *The Hill*. A native of Sarajevo, he earned his B.A. and M.A. degrees from the Rubin Academy of Music in Jerusalem and his Ph.D. in music from the Academy in Lovran, Croatia. He is also the recipient of the UNESCO Artist for Peace title.

**Boris Tučić** is the head of the Republika Srpska Prime Minister's Office. He held several positions throughout his career, including the minister of foreign trade and economic relations of Bosnia and Herzegovina. He holds a Ph.D. in Political Science with a focus on European Studies, and has primarily focused on the European integration process, the legal, institutional and political nature of the European Union and its policies, and the stabilization and association process of the Western Balkan countries. Tučić is the author of two monographs and several dozens of research papers.

**Artur Turemka** is the General Manager for the Balkans at Mastercard, and is responsible for the development of regional business and market strategy for seven highly dynamic Balkan countries: Albania, Bosnia and Herzegovina, Bulgaria, Kosovo, Macedonia, Montenegro, and Serbia. He oversees local strategies for achieving sustainable growth focusing on financial inclusion initiatives and implementation of innovative technologies, building on strengthening customer and governmental relations. Turemka has held this position since 2013, prior to which he built extensive experience both within Mastercard and in banking and automotive industries. He holds a Master's degree in marketing and management from Warsaw University in Poland, and studied Business Administration at Graz University in Austria.

**Lars-Gunnar Wigemark** is the Head of the Delegation of the European Union to Bosnia and Herzegovina and the European Union Special Representative in Bosnia and Herzegovina since April 2015. From February 2011 to March 2015, he served as the Ambassador and Head of the European Union Delegation to Pakistan. In 2008, Ambassador Wigemark was appointed Head of the Security Policy Unit at the European Commission. He joined the Swedish Ministry for Foreign Affairs in 1988 and has been posted to Belgrade, Washington D.C., Brussels, Kabul, and Moscow, where he served as Minister and Deputy Head of Mission at the Embassy of Sweden (2003-2007). He graduated from Harvard University and holds a Master's Degree from the Fletcher School of Law and Diplomacy in International Law and Economics.

**Jane Wilson** is an international attorney and consultant who has specialized in energy sector reform for 30 years, working internationally for most of her career, in approximately 35 countries in South America, Asia, Africa and Europe, establishing policies and regulations related to energy sector restructuring and developing competitive protocols. Most recently, she worked and lived in Bosnia and Herzegovina for 11 years, managing energy reform and energy efficiency technical assistance projects for the United

States Agency for International Development (USAID). Currently, she works as a legal and regulatory expert for the USAID Energy Investment Activity Project in Bosnia and Herzegovina. Prior to working overseas as Vice President of Regulatory and Government Affairs for two U.S. international energy multi-national corporations (Enron and Entergy), Wilson held legal and line management jobs in U.S. natural gas pipelines. Earlier in her career, Wilson worked as a litigation attorney in private practice. Wilson has a joint Juris Doctor and Master's Degree in International Studies from the University of Denver.

**Muhidin Zametica** has been an Executive Director in a public company located in Sarajevo since 2008, and has been engaged in several projects implemented by the non-profit organization Green Council, most recently with the development of the Feasibility Study for a project on the production of thermal insulation materials made from sheep wool (2016). He retired in 2007, with the military rank of Colonel. Zametica worked as a Financial Manager in the BiH company "Energoinvest" until 1990, after which he set up and managed a private finance consulting firm in Sarajevo. Following the 1992-1995 war, Zametica worked as the Head of the Department for planning and budget at the BiH Ministry of Defense. Zametica coordinated the preparation of all defense budgets up until his retirement. He was directly engaged in development of policy for management of defense resources, concept and procedures for the system of planning, programming and budgeting, implemented in the defense system institutions in BiH. From 2000 to 2002, Zametica was a member of the Supervisory Board for the project of public accounting reform and introduction of the treasury system in BiH institutions. He was a member of several Steering and Supervisory Boards in public companies in BiH. Zametica graduated from the School of Economics within the Social Economy Department at the University of Sarajevo.