

31st Report of the High Representative for Implementation of the Peace Agreement on Bosnia and Herzegovina to the Secretary-General of the United Nations

Report to the United Nations Security Council

1 July 2006 – 31 March 2007

SUMMARY

The general election campaign and the subsequent negotiations to form new governments at the state, entity and cantonal levels dominated the second half of 2006 and the first quarter of 2007 in Bosnia and Herzegovina (BiH). Although I continued to encourage and support the domestic authorities in their efforts to adopt and implement the reforms required if BiH is to make further progress towards Euro-Atlantic integration, both the intense pre-election environment and the complicated post-election situation were far from conducive to success. By year's end, only Republika Srpska (RS) had a reconstructed government. The state-level Council of Ministers was formed in February, and a Federation government was finally established only on 30 March. At the end of March, six months after the elections, three of the ten cantons remained without new governments.

1. The highly divisive and occasionally inflammatory rhetoric that characterised the election campaign put my resolve to promote domestic ownership to the test; but it also made it

possible to make a realistic assessment of the extent to which the domestic political establishments could take on ever-increasing responsibility for their own country's affairs. Only by establishing the reality of the situation in BiH did it prove possible to identify the mechanisms that will be required in future to assist this country in completing its transition from post-communist and post-war fragility to Euro-Atlantic integration and security.

2. Despite repeated calls during and after the election campaign for a referendum on Republika Srpska independence – and countervailing demands from the Federation to abolish that entity – these first general elections since the war to be wholly organised and run by the domestic authorities passed off peacefully and successfully on 1 October. On the other hand, the parties that employed the most vociferous rhetoric during the campaign were also the biggest winners: the Alliance of Independent Social Democrats (SNSD) of RS Prime Minister Milorad Dodik and the Party for BiH (SBiH) of newly elected Presidency member Haris Silajdzic. The electoral arithmetic meant, however, that these two parties, regardless of their opposite stands on numerous issues, were compelled to share power at state level, in the Federation and in some cantons.

3. The other notable result of the elections was the weakening of the traditional nationalist parties that had dominated the political scene in BiH since the first free elections in 1990: the (Bosniak) Party for Democratic Action (SDA), the Serb Democratic Party (SDS) and the Croat Democratic Union (HDZ BiH). Their loss of predominance among their respective electorates does not signal, however, any diminution in the salience of national (and nationalistic) issues.

4. Little progress was made during the period in meeting the preconditions for signing a Stabilisation and Association Agreement (SAA) with the European Union. The technical

negotiations with the European Commission (EC) were completed successfully, with very good performances on the BiH side by both the chief negotiator and the Directorate for European Integration. However, the failure to forge a political agreement on police restructuring precluded the initialling of an SAA during the period.

5. Constitutional reform remained a high-profile issue, although there has been no concrete progress on constitutional reform during the last six months, primarily due to the focus of the local authorities on government formation and police reform. The package of amendments narrowly defeated in the BiH Parliament in April 2006 remains on the table. However, it appears increasingly unlikely that the package will get the necessary support to be reintroduced and adopted, despite clear and repeated calls for this by the PIC Steering Board. Recent political developments have confirmed constitutional reform as imperative for BiH for both political and functional reasons. The debate on BiH constitutional problems and the need for reform continue to consume much political and public space. BiH political leaders have recently started to promote some ideas on possible constitutional set ups. The 26 February ruling by the International Court of Justice on the suit launched by the former Republic of Bosnia and Herzegovina against the former Federal Republic of Yugoslavia in 1993 has brought the issue to the fore once more. Bosniak politicians, led by Haris Silajdzic, have seized upon the court's verdict and have pointed out that it was the army and police of the wartime RS that committed genocide in and around Srebrenica in July 1995. They demand both that the Srebrenica municipality should be removed from RS jurisdiction and that the RS itself should be abolished through more far-reaching constitutional changes. Their Serb counterparts have responded by both defending the legitimacy of the RS and offering economic and fiscal assistance to Srebrenica residents, the Bosniak returnees among whom have threatened to leave the town once more if their demands are not met. In close coordination with

the US government, in my capacity as EUSR, I am preparing for a broad constitutional reform process to be set up and operating in the second half of 2007.

6. In November NATO invited BiH to join its Partnership for Peace (PfP), together with Serbia and Montenegro. NATO Secretary General Jaap de Hoop Scheffer stressed in the aftermath of the decision that NATO still expected the three countries to improve their cooperation with the ICTY.

7. In December BiH scored another success when, after hard negotiations over agricultural imports with its neighbours, it joined the Central European Free Trade Agreement (CEFTA). Just as PfP is an anteroom to full NATO membership, CEFTA provides the Western Balkan states with a single set of EU-harmonised trade rules. Meanwhile, economic growth remained healthy, with an increase in real GDP (despite the one-time boost in inflation to 6.8 per cent following the introduction of VAT) and rising exports.

8. The security situation was stable during the reporting period. Only a few security incidents or cases of nationally motivated violence or vandalism were noted. The most serious took place around Mostar and in areas of Bosniak return to the RS during the summer.

9. Political processes in Mostar hardened in the second half of the year. No progress had been made by summer in finalising the systemisation of the administration, forming an urban planning institution, resolving the status of Hercegovacka Radio-Television and various cultural institutions, or forming a single public utility company. I therefore appointed a special envoy, Mr Norbert Winterstein, to mediate, arbitrate or recommend other solutions to outstanding disputes. He successfully resolved several of these longstanding issues, but I was required in December to impose solutions pertaining to urban and spatial planning that he had recommended but had been unable to convince the

polarised parties to adopt.

10. Brcko District was also characterised by mounting party disputes within the majority coalition and declining effectiveness on the part of the government, all exacerbated by the state-wide election campaign, uncertainty over the District's post-supervisory future, and continuous disputes over revenue allocation from the BiH Single Account. Dr Raffi Gregorian succeeded Mrs Susan Johnson as Supervisor in September, just in time to take part in the negotiation of a state law on Brcko District that will seek to regulate the District's long-term status and prerogatives. Dr Gregorian also instituted changes to the District's Statute that will make for more functional and accountable government.

11. As noted above and predicted in my previous report, the uncertain regional situation and, in particular, mounting tension occasioned by both the approach to and deferment of a Kosovo status decision impacted unhelpfully on BiH politics and political discourse over the period. The independence referendum in Montenegro in May set the scene for much loose and inflammatory talk of both "self-determination" in Republika Srpska and abolition of the entities in the Federation during the election campaign. This continued as Belgrade officials attempted to link the fates of Kosovo and the RS. Prime Minister Dodik also used the renegotiation of the parallel relations agreement with Serbia, Belgrade's offer to build a new bridge across the River Sava at Bosanska Raca, and the lucrative sale of the entity's telecommunications operator to its state-owned Serbian counterpart to reinforce his close economic and political connections with Serbia.

12. OHR staff continued to work towards fulfilling the OHR Workplan and revised Mission Implementation Plan (MIP) that were approved by the Peace Implementation Council in March 2006. Our efforts were hampered, however, both by pre-election politicking and by the post-election interregnum as parties slowly negotiated the formation of new coalition

governments. The Workplan and MIP completion rates suffered accordingly.

13. It is this uncertain regional environment, combined with the virtual halt in reform and the prolonged void in government following the elections, that convinced me that it would be rash to proceed with the planned closure of OHR and transition to a solely EUSR operation in BiH after June 2007. The Peace Implementation Council Steering Board endorsed this view at its meeting in Brussels on 26-27 February. In line with the general consensus of PIC Steering Board members, there was agreement to aim for OHR closure by 30 June 2008 and to review the situation in October 2007 and February 2008. The PIC Steering Board underlined that the policy of ownership remains the guiding principle and that the International Community will help Bosnia and Herzegovina to make the final steps from peace implementation to Euro-Atlantic integration as soon as possible. Russia stated that it was unable to join this consensus and that it would make conclusions consistent with UN Security Council Resolution 1722. I had announced in January that I would not seek an extension of my mandate beyond June 2007.

I. Introduction

14. This is my second report to the Secretary-General since assuming the office of High Representative for Bosnia and Herzegovina on 31 January 2006. As has been the norm, it assesses progress made towards attaining the goals outlined in previous reports, reviews developments during the reporting period and provides my assessment of mandate implementation.

II. Political Update

15. The results of the 1 October general elections were certified on 27 October – a few days before the legal deadline – but the broad contours of the resulting political landscape in BiH had been far more quickly discernible. The big winners

were Milorad Dodik (and his SNSD) and Haris Silajdžić (and, to a slightly lesser extent, his SBiH). Their victories were also victories for the radical and polarising political rhetoric they had employed during the campaign, which had centred on their antithetical conceptions of the future constitutional order in BiH. The irony of the result is that their two parties are now condemned to cohabitation in government and future progress will largely depend on the ability of Dodik and Silajdžić to find mutually acceptable compromises.

16. The other notable result of the October poll was the blow administered to the 'big three' nationalist parties – the SDA, SDS and HDZ BiH – that had dominated their respective people's political horizons since 1990. Although diminished in strength, all three will, however, continue to be important players. In fact, only the SDS will be excluded from a share in power at the state and entity levels. The traditional nationalist parties' relative or absolute defeats did not mean, of course, a defeat for nationalist politics. The victors simply proved more adept at mobilising national sentiments and issues, accusing the formerly dominant nationalists of having failed to stand firm on salient national issues such as constitutional reform and the balance between state and entity prerogatives.

17. With 41 out of the 83 seats in the RS National Assembly, Dodik came close to winning an absolute majority and more than doubled the SNSD's previous 19 seats. The SDS, by contrast, saw its tally fall from 26 to 17 seats. It promptly repudiated its latterly moderate leader and defeated candidate for re-election as RS president, Dragan Čavić, and turned to the right. Dodik, for his part, needed only to offer ministerial office to a few smaller parties to construct a strong majority and, then, to reshuffle his existing cabinet. Having done so, he won confirmation by the RSNA on 29 November.

18. In the Federation the SDA retained its position as the biggest Bosniak party with 28 seats in the lower house, but this loss of just four mandates understated the party's relative defeat in the face of the SBiH's jump from 15 to 24 seats and Silajdžić's clear victory over SDA leader Sulejman Tihić in the race for the Bosniak place on the BiH Presidency. The long-dominant Croat party, the HDZ BiH, lost half of its previous 16 seats in the Federation lower house, but still edged out the breakaway HDZ 1990, which won seven. On the other hand, the HDZ 1990, in combination with smaller Croat parties, claimed leadership of the majority Croat coalition once all the cantonal assemblies had elected their delegates to the upper house, the House of Peoples.

19. A feature common to both entity parliaments elected in 2006 is that the number of parties winning seats was reduced, so making political management easier. No Croat parties, for example, won seats in the RSNA, though the number of Croat deputies (elected as SNSD candidates) remained the same at four. The number of predominantly Bosniak parties winning seats in the RSNA remained the same (three), but their total number of seats fell from ten to eight. On the other hand, the SNSD won two seats in the Federation parliament.

Government formation

20. The SDA and SBIH leaders quickly agreed in October on an undefined post-election coalition, but serious talks about forming a state-level government did not begin until mid-November. They continued in desultory fashion until year's end, but picked up speed and purpose in January. The major sticking point throughout was which of the two HDZs would share power, since the SDA preferred the HDZ BiH and the SBiH wanted a partnership with the HDZ 1990, which had also opposed the March set of constitutional reforms. For its part, the HDZ BiH long rejected any notion that both Croat parties should enter government. In the end, the Council of Ministers confirmed by parliament on 9 February and the Federation

government finally established on 30 March contained ministers from both Croat parties.

21. Despite the fact that the business of forming the state and Federation governments was long and tortuous, it was a positive sign that the SNSD was determined both to occupy the prime executive post at state level, so according the chairmanship of the Council of Ministers enhanced importance, as well as to take ministerial office in the Federation for the first time. In addition to the chairmanship of the CoM, the SNSD took two of the more important state-level ministries. It was an equally healthy sign that there were no demands that the international community should intervene to broker a deal. Although Dodik stated before the CoM was established that the governing majority would be a purely mathematical combination – not a real coalition – and that the SNSD would focus on running ‘its’ ministries, his interest in the chairmanship and the calibre of his ministerial nominees hinted otherwise.

22. Although the six parties that signed up to the March 2006 package of constitutional reforms won the two-thirds majority of seats that would be required to pass the amendments on a second attempt, two (the SDP and SDS) have gone into opposition and announced that they can no longer be counted upon to back the amendments, while a third (the SDA) is internally split on the issue. The combination in government of parties wholly opposed to the package (SBiH and HDZ 1990) with those who still favour it (SNSD and HDZ BiH) and one that is now equivocal (SDA) means that no clear way ahead is yet visible. The PIC Steering Board nonetheless reaffirmed its view that early adoption of the package would constitute a positive first step and provide a basis on which to establish a broader process by mid-2007 that would help Bosnia and Herzegovina meet the requirements of a modern European state.

23. As noted above, the new but little changed RS government was confirmed in office on 29 November, celebrating in mid-

March the achievements of its first 100 days while Federation politicians were still wrangling over portfolios – and particularly those to be allotted to the Croat parties. Once this was done, there followed a rushed attempt on 22 March to subvert the process whereby my office vets nominees for five sensitive ministries. The ostensible reason for the sudden haste was the need to adopt and enact the Federation's 2007 budget before the expiry of the temporary financing authority on which the caretaker government had operated.

24. Having warned parliamentarians that vetting was not yet complete and asked them to postpone their session for the day or two that would be required, the House of Representatives nonetheless proceeded to elect the new government. I was thus compelled to nullify the House's vote on 23 March. Since one ministerial candidate did not, in the event, pass the vetting procedure, I asked the relevant party (the SBiH) to nominate another. This it promptly did, so permitting an accelerated vetting procedure and a new session of parliament on 30 March. The cabinet was duly confirmed and the 2007 budget passed.

25. The new Federation House of Representatives had convened within the prescribed deadline on 21 November, but did so only to swear in MPs and to recess. Most cantonal assemblies did not even do that. Moreover, the cantons' failures to respect deadlines made it impossible to form the Federation House of Peoples (which is elected from the cantons) and the BiH House of Peoples (two-thirds of whose members are elected from its Federation counterpart) before February. In addition, there will continue to be a small 'deficit' of Serbs in the Federation House of Peoples, since not enough were elected to the cantonal assemblies. Moreover, three cantons remained without new governments at the end of March.

Party-political realignments and reactions

26. The immediate post-election period saw the weakened

leaders of the SDA and SDS facing revolts over their parties' disappointing results. While Tihić (SDA) survived, Čavić (SDS) was forced out in mid-November. The SDS has now reverted to the intransigence of its earlier days, but is unlikely to be able to outflank Dodik in this regard. The newly elected SDS leadership has nevertheless been openly flirting with former SDS officials removed for support of "Persons Indicted for War Crimes" (PIFWCs).

27. The new HDZ 1990 bucked the trend established by earlier breakaway parties from the HDZ BiH in winning a substantial number of seats at the state, Federation and cantonal levels. The HDZ 1990 benefited from perceptions that it was backed by both the HDZ government in Zagreb and the Catholic Church, as well as from the conviction in the autumn of HDZ BiH leader Dragan Čović for financial crimes when he was Federation finance minister.

28. The major non-nationalist (or non-national) party, the Social Democrats (SDP), failed to make significant headway, but is set to remain the strongest opposition party in the state and Federation parliaments. The party's one success, the election of its candidate, Željko Komšić, to the Croat seat on the Presidency stemmed from the split between the two HDZs and the votes of SDP loyalists among all three constituent peoples. The explicitly Croat parties cried foul and denounced the legitimacy of a Croat supposedly elected by non-Croats, but their protests petered out rapidly. SDP leader Zlatko Lagumdžija subsequently called for a vote of confidence in his leadership, which he won easily.

29. Claims by Dodik that the secessionist rhetoric that characterised the campaign in the RS would evaporate after the election have, by in large, been borne out by events. On 28 March, RS President Milan Jelić stated that the SNSD had abandoned their pre-election rhetoric on an RS referendum as the international community and OHR have clearly said that the RS could not be abolished and so there was no need for a

referendum. The RS prime minister did, however, keep the notion of a referendum alive by proposing instead to call one on policing should the existence of the RS police be threatened. (This was an idea he borrowed from the SDS). RS-based NGOs, however, have continued to agitate on behalf of referenda on both policing and secession.

Constitutional Reform

30. As noted above, the future of the first-ever package of constitutional amendments in post-Dayton BiH remains uncertain. Nonetheless, constitutional reform was an inescapable subject during the coalition negotiations and will remain on the agenda no matter how divided the new governments may be on the issue. Although nearly everyone agrees that constitutional change is necessary if BiH is to have functional, affordable and EU-compatible governance, few agree on the nature and scope of the reforms. Most Serbs want an explicitly federal state composed of three 'national-majority' units, though any effort to define the prospective boundaries of such units undermines potential Serb-Croat concord on this point. Bosniaks, on the other hand, continue to favour an integral or 'civil' state, the territorial sub-units of which would be merely administrative – and certainly not national or constituent. This is unacceptable to Serbs and Croats because they see it as guaranteeing majority, that is, Bosniak rule.

31. Bosniaks' determination to pursue the goal of an entity-free BiH has been reinforced by the International Court of Justice's 26 February verdict. The court's finding that the wartime institutions of the RS were responsible for genocide in Srebrenica has provided an opening: first for demanding Srebrenica's removal from RS jurisdiction, then for the elimination of the RS police and, eventually, for the abolition of the entity itself.

32. Although both the US government and I had hoped to work for speedy adoption of the modest package of amendments that

failed in April, making it clear that this was but the first step in what would have to be a more thoroughgoing process of constitutional reform, the omens are far from good at present. In the medium term, however, both the pressure of events and the development of a popularly inclusive procedure involving the BiH Parliament, outside experts and civil society could forge the necessary consensus for change. This will require an effective structure, combining both international and Bosnian experts, and a strong secretariat to support the BiH Parliament and maintain momentum. There will thus be a key role for the international community to play, particularly the EU, led by the EUSR and the US, in supporting the initiation of this process and facilitating progress over the next few years.

33. Also on the constitutional front, I was obliged on 23 March to issue an order to assure the integrity of decisions taken by my predecessors and myself and to make sure that the authorities of Bosnia and Herzegovina abide by their obligations under the Dayton Peace Accords and UN Security Council resolutions. The need for this order arose from a July 2006 ruling by the BiH Constitutional Court on an appeal for redress from two persons removed from office by my predecessor in 2004 in relation to non-cooperation with the ICTY. The court, although not directly challenging this decision, had ordered the state authorities to take steps to establish a remedy for such removal decisions. My order establishes a process whereby the authorities will be able to comply with the Constitutional Court's ruling without, at the same time, violating their obligations to respect and implement decisions of the High Representative taken under Annex 10 of the General Framework Agreement for Peace. The order prohibits the establishment of any review mechanism by the BiH authorities while obliging them to refer such matters to the High Representative, as Chair of the Peace Implementation Council Steering Board.

34. This order was made following close consultations with PIC Steering Board members and others. On 27 February the PIC Steering Board had reminded all institutions that Bosnia and Herzegovina's international obligations under the GFAP and the United Nations Charter must be respected and called upon me to take appropriate actions to ensure that BiH fulfils these international obligations.

III. European Partnership Requirements

35. The technical rounds of SAA negotiations completed in 2006 proved constructive. Their focus was on trade concessions, the movement of goods, approximation of laws, law enforcement and competition rules, mutual assistance in customs matters, dispute settlement mechanisms, and transitional periods. No breakthroughs were made, however, on the preconditions for signing a SAA: police restructuring, public broadcasting reform and ICTY cooperation.

Police Restructuring

36. In December 2006, the Directorate for Police Restructuring Implementation ("Directorate") completed its 36-page final report, "Proposed Plan for the Implementation of the Reform of Police Structures in Bosnia And Herzegovina," as mandated by the October 2005 Agreement on Restructuring of Police Structures (Political Agreement). The Directorate submitted its report to the BiH Ministry of Security on 27 December 2006 and on 3 January 2007 the Ministry of Security forwarded it to the secretary general of the caretaker Council of Ministers.

37. The report was the result of 12 months' work, during which the Steering Board of the Directorate held 28 meetings (15 during the reporting period). There were numerous delays, however, stemming largely from the RS government's obstruction of and objections to the legitimacy of the process, notwithstanding the fact that the RS National Assembly had

adopted the Political Agreement and Serb ministers in the CoM had supported the formation of the Directorate. RS opposition to the process culminated in a decision in May 2006 to downgrade RS representation on the Steering Board to that of observer. Directorate members from RS institutions maintained their status as observers for the remainder of the Directorate's mandate, although Serb representatives of the state continued to participate.

38. As a result of these delays and obstructions, the report was submitted three months after the deadline foreseen in the October 2005 Political Agreement and minus some of the elements specified by that agreement. In particular, it does not include draft legal acts or rulebooks, a timetable for the overall implementation period, or a map of police regions.

39. The proposed policing system provides for an organisationally integrated structure with decentralised police operations and decision-making. The consolidation of administrative services (human resources, finance, procurement, IT/communications), which are currently duplicated in each of the existing fifteen police forces, is perhaps the most far-reaching aspect of the report. The new system also envisages a single forensics centre and police academy. The local policing level would operate with fairly extensive autonomy, although the future Director of Police and the Directorate for Police Coordination would provide an operational hierarchy.

40. The report also offers concrete solutions designed to implement the three guiding principles set by the European Union:

1. *All legislative and budgetary competencies for all police matters must be vested at the state level.*
2. *No political interference with operational policing.*
3. *Functional local police areas must be determined by*

technical policing criteria, where operational command is exercised at the local level.

41. As for the first principle, the report clearly establishes that the state should be vested with exclusive legislative competency for all police matters and that other levels of government cannot legislate on police matters. The report also envisages a single police budget to be adopted by the BiH Parliamentary Assembly. Regarding the second principle, the report provides for numerous oversight mechanisms designed to keep politics out of policing, mainly through parliamentary watchdogs and institutions such as the Independent Board and Public Complaints Office. On the third principle, the report enumerates specific technical guidelines and criteria for forming local policing areas, but it does not contain a map suggesting what they should be.

42. In line with the Political Agreement, the state and entity governments and parliaments will need to adopt the Directorate's proposal, along with any agreed amendments. Because of the earlier withdrawal of RS support from the Directorate, continuing Serb determination to maintain the RS name for police forces deployed on its territory, and a reinforced Bosniak view that no such thing must happen, the forging of a political consensus on the Directorate's report, let alone the number and shape of local policing regions, has thus far proved impossible. My office has organised or participated in numerous meetings among party leaders this year, as well as conducting bilateral negotiations.

43. At several points it has looked as if progress was being made, most notably at a meeting of Serb and Bosniak leaders on 14 March, the day before EU Enlargement Commissioner Olli Rehn arrived in Sarajevo. Although Dodik on that day shifted his position significantly towards meeting the three EC principles, Silajdzic and Tihic deemed this to be insufficient, offering compromise only after Rehn had left and

Dodik had back-tracked. Failure to reach political agreement and, then, quickly to translate such an agreement into parliamentary acts and legislation on implementation may make it increasingly difficult for BiH to sign a SAA before the end of 2007.

IV. Entrenching the Rule of Law

44. In addition to police reform, my office has continued to focus on facilitating and consolidating the implementation of other rule of law reforms, especially those that aim to build the capacity of existing law enforcement agencies and the BiH State Court.

45. OHR/EUSR has worked over the period with the BiH Ministry of Security, the State Investigation and Protection Agency (SIPA), the State Border Service (SBS) and the entity and cantonal interior ministries and police to build their capacity, particularly in the fight against organised crime. We have also worked to enhance the capability of the recently formed BiH Service for Foreigners' Affairs.

46. In the second half of 2006 my colleagues sought to identify systemic problems in the work of prosecutors and to facilitate improved cooperation between them and the police. They also produced an analysis of strategies and best practices in the prosecution of organised crime in other European countries and distributed it to local prosecutors.

47. OHR contributed as well to ensuring a successful transition by the Registry of the State Court to full domestic ownership by concluding a new registry agreement. Replacing the December 2004 original, the new agreement provides for a gradual transfer of responsibility for the Registry to domestic institutions. Of particular importance are the provisions which give authority to the High Judicial and Prosecutorial Council to appoint all judges to the State Court and all prosecutors to the State Prosecutor's Office, as well

as provisions reorganising the Registry and its financing. The agreement also provides for the integration of national Registry staff into domestic judicial institutions between 2006 and 2009. The goal is to ensure that BiH assumes full responsibility for the State Court and Prosecutor's Office in regard to finance, administration and personnel matters, as well as to guarantee the long-term sustainability and capacity of domestic judicial institutions to process war crimes and organised crime cases.

V. Cooperation with the ICTY

48. A number of complex trials for war crimes remain underway in the State Court. The court also initiated trials of cases transferred from the ICTY in the reporting period (Savo Todović, Mitar Rašević and Paško Ljubičić). The first instance verdict in another case transferred from The Hague (Radovan Stanković) was handed down in November, with the accused being found guilty of crimes against humanity and sentenced to 16 years' imprisonment.

49. There was little or no progress in capturing remaining ICTY fugitives. In December, however, the RS government adopted a new Action Plan directed at the location, apprehension or voluntary surrender of ICTY fugitives. We shall be looking forward to seeing it implemented. In the meantime, my colleagues and I will continue to monitor and exhort the authorities in BiH, in particular the RS authorities, in this matter.

50. In addition to its 27 February decision not to close OHR in June 2007, the PIC Steering Board directed OHR to reinforce its efforts to secure full cooperation with the ICTY by the domestic authorities during its remaining tenure. My office is making every effort to do so, all the more so because of the simultaneous judgment of the International Court of Justice and the political impact it has had in BiH.

VI. Reforming the Economy

51. Now that the new governments are in place it is imperative that they should both rise to the challenges ahead and deal with a substantial backlog of essential fiscal and economic legislation. The country not only needs to maintain sound macroeconomic policies, but it must also make substantial progress on the structural reforms required to lay the foundations for sustained, private sector-led growth.

52. That said, economic growth has remained relatively robust, and it is likely that real GDP growth of 5 per cent in 2005 will increase to 5.7 per cent in 2006. The introduction of VAT inevitably impacted on retail prices, producing a one-time rise in the average rate of inflation to 6.8 per cent. Exports have picked up and, with improved statistics, the current account deficit should show a narrowing from 21 per cent of GDP in 2005 to about 13.5 percent of GDP in 2006. The external deficit, however, remains very large.

VAT Introduction

53. The successful introduction of value-added tax was the undoubted high point of economic reform in 2006. Projected revenue collection from VAT for 2006 was KM 3.5 billion. Actual revenues far exceeded the initial projection, reaching a final total of slightly more than KM 4 billion. There continues to be intense disagreement, however, over the formula for allocating these revenues among the entities and Brcko District, making it clear that the current methodology represents a constant source of contention. As a consequence, revenues from the Single Account have only been allocated on a monthly or bi-monthly basis, and sometimes in arrears. This contention has also caused delays in reaching an agreement on the National Fiscal Council, which still has no basis in law and has, therefore, neither an effective mechanism for breaking deadlocks among its members nor any means of enforcing its decisions.

Budgets

54. The effects of the unsatisfactory level of intergovernmental coordination and the lack of a law on the National Fiscal Council were again obvious. Preparation of the 2007 budgets continued to be marred by such weaknesses. Governments are boosting their spending in an inefficient and shortsighted manner, albeit not dangerously. But this tendency poses a fiscal risk if revenues stagnate, let alone drop, for the governments quickly came to rely on steadily increasing revenues during 2006.

Business Environment

55. Progress in improving the business environment, restructuring corporations and making structural reforms slowed in 2006. According to the World Bank Business Environment and Enterprise Performance Survey 2006, improvements have mainly been made in taxation, customs and trade regulation. However, all efforts to centralise banking supervision at state level or to adopt laws crucial for creating a single economic space in BiH (e.g., laws on obligations and pharmaceuticals) have failed or been postponed. My office has also been engaged in improving the business environment through institutional support for business associations and trade chambers, as well as in encouraging socio-economic dialogue.

56. Corporate restructuring has proceeded slowly and progress in strengthening corporate governance has been modest in comparison to neighbouring countries. The absence of political interest or will has stymied significant privatisation efforts in the Federation, although there has been significant progress in the RS in privatising a number of large companies.

Infrastructure reform

57. While the demand for most modes of transport is growing

markedly, the absence of an overall national infrastructure policy is a major problem. This is partly due to the lack of institutional capacity, but also to politics, particularly in the railway sector. The situation is slightly better in the electricity industry, which has been restructured with significant assistance from the World Bank, European Commission and several other donors. The main challenges will be to increase the power-generation capacity in a transparent and competitive process with the objective of achieving a balance between risks and benefits, both for BiH and investors.

VII. Public Administration Reform

58. The state, entity and Brcko District governments adopted the National Public Administration Reform (PAR) Strategy prepared by the BiH PAR Coordinator during the reporting period. Six inter-governmental working groups were established to work on its implementation. The strategy encompasses the six horizontal PAR areas: human resources, legislative drafting, administrative procedures, information technology, institutional communications and public finance. OHR provided both political support and technical assistance throughout the adoption process.

59. Although the working groups have been set up, implementation of the action plan has yet to begin in earnest. This will need to be the focus in coming months, and OHR will, within its means and capabilities, seek to assist the authorities in doing so. Initiating the implementation of the comprehensive PAR action plan is a key short-term priority of the European Partnership and a condition for signing a SAA.

VIII. Defence Reform

60. NATO member states invited BiH to join the alliance's Partnership for Peace (PfP) on 29 November 2006. This signified fulfilment of one of the main benchmarks of success

in defence reform. Meanwhile, work continued throughout the period on transferring all property identified by the BiH Ministry of Defence as necessary for defence purposes from the entities to the state. This effort was hampered, however, by the RS government's repeated refusals to comply with the relevant provisions of the Defence Law. Work on transferring EUFOR's residual Dayton tasks and functions to the BiH authorities also intensified. But BiH remains in need of legislation providing for the oversight of movements of weapons and military equipment (WME) within the country, including the structures required to ensure implementation. The domestic authorities worked as well on programmes aimed at safely disposing of surplus WME. However, without transfers of ownership by the entities, these programmes cannot be implemented.

61. After much political wrangling and discussion of relative national representation in the Armed Forces of BiH (AFBiH), on 5 July 2006 the state Presidency finally adopted a decision on their size and structure that allows for the development of an increasingly integrated force. It thus offers a solid basis for future progress while providing immediately for the AFBiH to have niche capabilities in the spheres of de-mining and explosive-ordnance disposal. There is a realistic ratio of officers to non-commissioned officers and soldiers (2:3:5). The force will be fully professional, with no conscripts and no passive reserve. PfP membership will help ensure that improvements continue to be made, particularly since BiH has begun to participate in the NATO force-development process. The BiH Chief of Joint Staff has produced an implementation plan with timelines for the stand-up of all elements of the AFBiH. This plan aims to ensure that the legally defined dates for the formation of headquarters and the battalions assigned to them can be met. It is likely, however, that these timelines will slip, owing to the fact that the selection process for military personnel is not yet complete.

62. BiH submitted its Presentation Document to NATO before the end of 2006. It has been accepted and BiH is now preparing its Individual Partnership Plan. On 16 March 2007 BiH also signed a NATO Security Agreement that defines parameters for the exchange of information between NATO and BiH, including document handling, security clearances and the like. The initial phases of the Planning and Review Process have also begun.

63. Although not a defence-reform issue *per se*, BiH recently dispatched its fifth contingent (an Explosive Ordnance Disposal platoon) to serve with the US-led coalition in Iraq. Each contingent has served for six months. Platoon members are volunteers drawn from the AFBiH as a whole and, as with other, smaller deployments in the past (e.g. with the UN in Ethiopia/Eritrea), they represent all three constituent peoples.

IX. Intelligence Reform

64. The BiH Intelligence and Security Agency (OSA) fine-tuned its organisational structure during the reporting period in order to take on the responsibility for security vetting prescribed by the Law on the Protection of Secret Data. A first batch of OSA employees commenced training on both operational and analytical aspects of the agency's work. Such training, as well as consultations with international experts, remained a priority. Both executive control and parliamentary oversight of OSA continued to mature.

65. OSA underlined its ability to act as the key point of contact in BiH for counter-terrorism efforts through its membership of several international forums for intelligence cooperation. Bilateral donors provided both training and material assistance. OHR will continue to work with the OSCE Mission to BiH and other partners to consolidate the agency's compliance with all aspects of the laws that regulate it and to ensure both proper executive control and effective

parliamentary oversight.

X. The European Union Military Mission (EU Force in BiH)

66. The European Union Military Mission (EUFOR) continued to conduct operations to ensure compliance with the General Framework Agreement for Peace and to maintain a safe and secure environment. EUFOR troops conducted a number of operations, including presence patrolling, observation activities, weapons' collections and specific operations targeted at the support networks of war-crimes indictees and associated criminal elements. Thanks to improvements in the security situation, EUFOR started to reduce and, in some areas, to end routine patrolling towards the end of 2006.

67. EUFOR maintained some 6,000 troops from 22 EU member states and 12 other countries. The force remained deployed in three regional multi-national task forces based in Banja Luka, Mostar and Tuzla, in addition to 44 Liaison and Observation Teams (LOT) throughout the country.

68. As a result of new common operational guidelines established between EUFOR and EUPM, EUFOR ceased to conduct independent operations targeting organised crime. Instead it backs up domestic law enforcement agencies when their requests for support are endorsed by EUPM. Having fulfilled its mandate, the EUSR-chaired Crime Strategy Group formerly tasked with overseeing the coordination and coherence of the EU's Security and Defence Policy in support of the BiH authorities' fight against organised crime closed down in November.

69. The EU decided in principle on 11 December to downsize EUFOR during 2007. The EU's Political and Security Committee confirmed this decision on 27 February. Implementation has begun and is due to be completed in the summer, when EUFOR will consist of some 2,500 troops in country. The new force posture that is planned provides for the retention of one battalion and two Independent Police Unit (IPU) companies,

based at Camp Butmir near Sarajevo, while additional battalions will be available 'over the horizon' to reinforce EUFOR at short notice. EUFOR will, however, maintain a countrywide presence in the form of LOT deployments, the purpose of which is to provide EUFOR with real-time situational awareness.

XI. Refugee and Displaced-Person Return

70. OHR handed over GFAP Annex 7 responsibility for refugee and displaced-person returns to the domestic authorities at the end of 2003, when property repossession was nearly complete. Property repossession has since been completed throughout the country, all municipalities having dealt with outstanding first instance applications for repossession of dwellings.

71. Permanent returns – and the sustainability of those returns – are, however, different matters. Unlike the number of repossessions, it is virtually impossible to offer a reliable estimate of the number of people who have returned physically to their pre-war homes. While the number of potential returnees grows ever smaller with the passage of time, a re-registration exercise undertaken by the Ministry for Human Rights and Refugees revealed that there are still 130,000 displaced persons in BiH who want to return to their pre-war homes. They need and deserve support, as do those who have returned but who often lead precarious lives. Field visits undertaken by OHR and UNHCR staff found that an alarming number of 'minority' returnees to rural areas lacked the rudiments of modern life, such as electricity and running water.

XII. Mostar

72. Persistent intervention by my office in the affairs of the city of Mostar was necessary in the second half of 2006. The political parties continued to stall or block the

reorganisation of the city administration, the formation of a single public utility company to cope with ongoing waste-disposal problems and any resolution of the status of the city-owned but Croat-controlled Hercegovacka Radio-Television (HRT). Moreover, the Croat-Bosniak dispute over urban planning threatened to create new parallel structures. All of these contentious issues continued to threaten the city's normal functioning and unity.

73. After the city authorities failed repeatedly to meet several deadlines I set for resolving these issues – as well as to take up the opportunity I offered them to settle the HRT dispute through arbitration – it became necessary by September to appoint a special OHR envoy to Mostar. I tasked the experienced Norbert Winterstein to try to build the political consensus necessary to make decisions, as well as to arbitrate in cases where no consensus could be forged. If even arbitration were not acceptable, I asked him to propose solutions to me.

74. Mr Winterstein soon succeeded in obtaining the consent of the city council to arbitrate the final status of HRT. He decided that HRT must be either transferred to new ownership or liquidated by 31 March 2007. On 30 March the City Council passed a decision to transfer ownership of HRT to three Croat-majority cantons, although they have not yet formally accepted such a transfer. Mr Winterstein also succeeded in brokering agreements on the formation of a single public utility company and in pushing ahead with the reorganization of the city administration.

75. Since urban-planning issues could not be resolved by compromise, as a last resort I issued two decisions on 22 December to establish urban and spatial planning bodies in the city. The Bosniak-dominated parties took these decisions as attacks on them and criticised them as biased.

76. Although Special Envoy Winterstein made significant

progress in securing agreements and proposing decisions, the difficult work of implementation lies ahead during 2007. Continued obstruction may leave me no choice but to use the Bonn Powers again. Mostar remains politically unstable, and will continue to require OHR attention.

XIII. Brcko District

77. Since 1999, when the Final Arbitral Award established Brcko District as a single, multi-ethnic administrative unit under an international supervisor, the district developed a political culture that was distinct from the rest of the country. Problems were solved locally, without recourse to national political parties, even after the first district-wide elections in October 2004. Lately, however, this has begun to change. The political radicalisation accompanying the general election campaign and the approach of the end of the supervisory regime combined to create a new and negative dynamic. Fearful of a future without a supervisor to check nationalist excesses, parties have been playing up ethnic issues that had hitherto stayed in the background.

78. Serb politicians were concerned during the period about the need to appoint a new police chief. They believed the chief should be a Serb because his predecessor had been a Serb, but also because Bosniak politicians were reportedly expressing the desire to get hold of major enforcement positions in the government, including the police chief (the acting chief was a Bosniak), the new auditor and the public attorney, in addition to the mayoral and prosecutor positions they already held.

79. Accusations of corruption and national discrimination have been bandied about without regard to facts or evidence. Bureaucratic inertia, laziness and incompetence are often mistaken for deliberate actions. The government has procrastinated in making preparations to create an independent Health Insurance Fund and Public Utility Company and initially

failed to provide for them in its draft 2007 budget. The District Assembly duly rejected it, displaying the dysfunctional relationship between the government and the assembly majority that has come to prevail.

80. Leaders already seem to be positioning themselves for the 2008 elections, both by raising nationalist issues and, increasingly, taking their cues (if not direction) from Banja Luka, Sarajevo or Mostar. This has had the effect of making some of the parties forming the governing coalition distance themselves from the work of their own government and not to support government proposals in the assembly, the better to pursue party and personal interests. The situation culminated on 28 December, when Bosniak councillors staged a walkout during the assembly's last session of the year in reaction to proposed reforms and the reallocation of positions resulting from government restructuring.

81. Outside influences on local political leaders are likely to intensify as the Supervisor's departure nears. The mayor could be weakened further, and may continue to rely upon the supervisor to compensate for the inadequacies of his government and bureaucracy. To counter these deficiencies, the Supervisor has focussed on increasing government accountability, performance and reform in order to diminish the impact of party politics on government services. Seven Supervisory Orders in February and March sought to promote this agenda. Dr Gregorian appointed a new police chief, restored two buildings to religious communities, amended the District Statute, appointed members of the Audit Office, and dismissed five officials dealing with urban planning issues. These actions have had a positive effect on restoring Brcko as a place of realised reform and great potential.

82. In November the Supervisor presented to the Brcko District Assembly the draft BiH Law on Brcko District and explained the process by which a joint working group had prepared it. The post-election interregnum precluded the

caretaker CoM from adopting and proposing the draft law to parliament. The new CoM now needs to do so, but it has also become evident that state and entity governments remain to be convinced that the law is adequate to the purpose.

83. Following a series of decisions that short-changed Brcko in terms of revenue, the Indirect Taxation Authority (ITA) Governing Board finally adjusted the revenue-allocation coefficients for December and January to reflect the final-consumption criteria when it met on 22 December. The re-balancing exercise for January-September 2006 returned nearly KM 7 million to Brcko. It remains to be seen, however, whether the final re-balancing, delayed as a consequence of there being no Federation finance minister, will restore all the funds that Brcko claims are owed. The district had meanwhile filed its submission asking for relief from the Arbitral Tribunal by the 30 November deadline. The submission complains that the ITA regime violates two principles of the Final Award. If the parties do not resolve their dispute in a timely fashion, it will be necessary to consider alternative solutions.

XIV. Bosnia and Herzegovina and the Region

84. As a multinational state whose three constituent peoples also inhabit its neighbouring countries, BiH cannot escape regional disputes or instability. Even the ordinary politics of Croatia, Serbia and Montenegro impact upon it. The RS government, in particular, has felt compelled to do Belgrade's bidding on numerous occasions.

85. As I have emphasised above, however, the uncertainty over Kosovo's future status and the delays in the announcement of the UN mediator's proposals had an especially baleful influence during the 2006 election campaign and thereafter. In fact, this risk of regional instability is a principal reason why I concluded that it would be rash to close OHR and renounce the Bonn Powers as early as 30 June 2007, the target

date set by the PIC in June 2006. Until such time as Kosovo's status is both settled and accepted – and arguments and passions attempting to draw BiH into the equation are moot and spent – fundamental changes in the nature of the international engagement in BiH must be considered carefully. The country may be peaceable and secure, but it is also vulnerable, both to external developments and their domestic reverberations, as well as to homegrown political instability. The reverberations set off by the 26 February verdict of the International Court of Justice are a case in point.

86. Any perceived diminution of international interest in BiH or any apparent weakening of resolve to uphold its sovereignty and territorial integrity could invite trouble. NATO's invitation to BiH to join PfP had a decidedly reassuring effect. Signature of a SAA with the EU would provide an even greater fillip

87. BiH still has minor border disputes with Serbia and Croatia, though the potential quarrel over Zagreb's plan to build a bridge between the mainland and the Peljesac peninsula that would have restricted BiH's access to the Adriatic seems to have abated. Another longstanding irritant to regional relations – the constitutional bars on extradition of their nationals by Croatia and Serbia – remains unresolved, although cooperation among prosecutors continues to improve. Bosniak politicians' efforts to call the dual-citizenship agreement with Serbia into question following Montenegro's departure from the state union and subsequent lack of interest in concluding a similar agreement with Croatia have lately been overcome.

XV. The European Union Police Mission

88. During the reporting period EUPM continued its successful work in co-locations with the local police. It implemented its refocused mandate and strengthened further its cooperation with EUFOR. With the Common Operation Guidelines in place,

EUPM took the lead in supporting BiH in the fight against organised crime and corruption, as tasked by the EU's PSC. The establishment of the Criminal Justice Interface Unit (CJIU) charged with addressing deficiencies in cooperation between police and prosecutors was a positive step. The CJIU focused on enhancing both general and case-specific cooperation in order to facilitate effective investigations and prosecutions, as well as to contribute to strengthening the integrity of the country's criminal justice system.

89. Pursuant to an operational review conducted at the end of the year, EUPM concluded that greater effort was required to support the ongoing battle against organised crime and corruption, including the provision of more hands-on advice regarding specific cases, in addition to general guidance.

XVI. Non-Certification of Police Officers

90. I continued during the period my efforts to help resolve the vexed issue of former BiH police officers denied certification by the United Nations International Police Task Force (IPTF) in 2002. The OHR/EUSR expert team returned to New York in July and met once more with EU Missions and with the UN Security Council Coordination and Drafting Group (CDG) and Department of Peacekeeping Operations (DPKO) to explore possible solutions. In August I wrote to the President of the Security Council and the Secretary-General, expressing my view that OHR/EUSR, in cooperation with the BiH authorities, had made every effort to provide the information required by the Security Council and DPKO and that it was up to the UN to take the next steps.

91. In November I reiterated this point in my speech to the Security Council and later in meetings with the Secretary-General and Under-Secretary-General for Peacekeeping Operations. In response to a November letter from the DPKO – and reflecting the mounting frustration and discontent in BiH over the continuing stalemate – I wrote again in December to

the Under-Secretary-General suggesting that it was incumbent upon our respective organisations to search for new solutions to this old problem. When former police officers embarked the same month on a hunger strike, the BiH Council of Ministers reacted by passing a unilateral decision to establish a *domestic* review process for officers denied certification by the IPTF. I called upon the CoM to respect fully its obligations under international law and pointed out that, were its decision to be implemented, I would have no choice but to consider further measures. I also called upon the CoM to contact the UN Security Council and the UN Secretariat as a matter of urgency. Since then, members of my staff have continued to consult with PIC Steering Board members, BiH institutions and others, including the Council of Europe.

XVII. Media Development

92. Efforts to complete public-broadcasting reform suffered a setback on 19 July at the hands of the Federation Constitutional Court, which ruled that the entity PBS law imperilled the “vital national interests” of Croats. In November the Bosniak club in the Federation House of Peoples appealed to the BiH Constitutional Court, seeking to reverse the entity court’s decision. The BiH Constitutional Court is not likely to rule on this issue before May.

93. If, however, that judgment is either unfavourable or further delayed, it will be necessary to introduce a redrafted law that meets the Federation Constitutional Court’s original and technical objections. In the meantime, OHR/EUSR will continue to meet regularly with the PBS governors and other stakeholders to discuss the course of reform and to encourage measures to modernise and streamline the system.

XVIII. The Mission Implementation Plan and the OHR Workplan

94. Thirty Workplan items remain outstanding. The PIC Steering Board asked me in February to revise the Workplan to

focus on remaining Dayton implementation requirements and on consolidating the reforms of state-level institutions necessary for the stability and sustainability of Bosnia and Herzegovina.

95. Work continued, however, on ensuring that Workplan items could be completed once the new governments were in place and normal legislative business resumed. In almost all cases the impediments have not been technical, but reflected an absence of engagement and determination on the part of the governing authorities. It remains to be seen how much political will the state and entity governments will prove able to mobilise. The fact that the blockage in the Council of Ministers following the ICJ verdict was overcome in mid-March – and some important decisions taken – may augur well.

XIX. EU Special Representative (EUSR)

96. In line with my dual mandate as European Union Special Representative in Bosnia and Herzegovina (Council Joint Action 2006/49/CFSP), I continued to promote the priorities listed in the European Partnership document of 2006, as well as the implementation of the GFAP. I also worked on behalf of constitutional reform, which remains essential to both rationalise and strengthen the country's governance and, by extension, to equip BiH for EU integration. In my EUSR role I also continued to provide political oversight of the European Union Police Mission. COMEUFOR, the EUPM commissioner and I agreed revised the terms of reference for the EU Crime Strategy Group during the reporting period.

XX. Reinforced EU Engagement in BiH and the Closure of OHR

97. OHR and EUSR members of staff worked towards meeting the conditions required for the transition from OHR to EUSR following the PIC Steering Board Political Directors' decision in June 2006 that OHR should prepare to close in June 2007. As I have emphasised throughout this report, however,

developments on both the regional and domestic scenes have been far from propitious, ultimately causing the PIC to decide on 27 February to maintain OHR. This means that OHR and EUSR will continue to work in tandem, but with the latter assuming increased prominence as the more leisurely transition process proceeds.

98. In the meantime the General Affairs and External Relations Council had on 16-17 October welcomed the second joint report by SG/HR Javier Solana and Enlargement Commissioner Olli Rehn on a reinforced EU Presence in BiH in the context of the closure of the OHR. In accordance with my mandate, on 23 November I submitted a detailed proposal for the consideration of the Council on the mandate, structure and resources required for a reinforced EU engagement in BiH. Working groups in Brussels examined the issues involved and the Council adopted a new joint action (legal basis) in January 2007. This will now need to be reviewed.

XXI. Reporting Schedule

99. In keeping with my proposal to submit regular reports for onward transmission to the Security Council, as required by Security Council resolution 1031 (1995), I herewith present my second regular report. Should the Secretary-General or any Security Council member require information at any other time, I would be pleased to provide an additional written update.