

**MACEDONIA'S PUBLIC SECRET:
HOW CORRUPTION
DRAGS THE COUNTRY DOWN**

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MACEDONIA'S PUBLIC SECRET: HOW CORRUPTION DRAGS THE COUNTRY DOWN EXECUTIVE SUMMARY AND RECOMMENDATIONS

Corruption in Macedonia, especially at high levels of government, is endemic. It has evolved from passive exploitation to active coercion and acquired the capacity not only to retard economic progress but also to feed organised crime and, in turn, political and communal instability. In effect, the state has come to function in important respects as a “racket”, while the racketeers thrive in a culture of impunity.

The disease has infected the banking system as well as the structures of government, making Macedonia both a source and a transit point for contraband and criminality. The system encourages autocratic administration while coexisting comfortably with inefficiency and politicisation of the judiciary. It saps Macedonian morale, leaving civil society enervated and the population at large cynical.

The Framework Agreement concluded at Ohrid in August 2001 cut short a rapidly evolving civil war but the agreement depends for its viability on the development of democratic institutions and a market economy. The corruption that eats away at the country is in many ways a cross-community, shared enterprise. At a minimum, it is highly damaging to the economy and increases the scope for social instability. However, it also invites outright collusion between ethnic leaders to heighten tensions and plays a substantial role in making the country ripe for conflict. Left to fester and spread, it will continue to erode Macedonia's tenuous unity and send dangerous ripple effects throughout the Western Balkans.

Unfortunately, the international community gives few indications that it recognises how powerfully

corruption works against its fundamental objectives in Macedonia. Officials typically excuse Macedonia with the empty phrase “corruption is a problem in all transition countries”. Occasionally, senior international officials issue high-minded demands for Macedonia to clean up its act, but these have never been seriously followed through. Opportunistic foreign investors sometimes exacerbate the problem.

The too frail international strategy emphasises “process” and “capacity building” – the passing of laws and the training of officials to, as one official says, “reduce the opportunities for corruption”. In the meantime, there is little effort to analyse why this approach has not produced meaningful results, why, for example, prosecutors do not act on ample evidence of corruption or precisely where criminal procedure loopholes allow corrupt officials to run free and keep their ill-gotten gains.

The international community insists that Macedonians take “ownership” of the problem, yet it is the “owners” themselves – those in powerful government positions – who continue to dominate, exploit and subvert its institutions. In current circumstances, it is both naïve and negligent to rely on weak indigenous watchdogs like the Ombudsman, the forthcoming Anti-Corruption Commission, or the media and civil society, to stand up alone to the corrupt elite. By pouring money into Macedonia without insisting on a serious anti-corruption effort, the international community is merely filling sink-holes in the budget and inadvertently acting as one of the system's enablers.

The argument is often made that “if we push them on corruption, the government won't cooperate on

implementing Ohrid". But failure to do so undermines the very agreement on which diplomats have concentrated their energies.

A dramatically different mind-set is needed. Macedonia is not "just another transition country" but an inherently weak state with external and internal challenges to its very existence. This means that corruption inflicts special damage and that, in effect, Macedonia can have either great corruption or stability but not both. Unconventional prescriptions are needed. To complement existing "capacity building" programs, the international community must incorporate fundamental changes in its approach. It must play the role of catalyst rather than simple adviser, unabashedly demanding reform if its financial assistance is to continue, and it must adopt a retrospective and punitive, not merely prospective and instructive, focus in its anti-corruption efforts.

Although this report contains specific examples, it has been written with care to respect the rights of individuals. ICG is prepared, however, to discuss a number of these matters in greater detail if requested to do so by appropriate, duly authorised governmental and legislative bodies.

Also, while this report deals with the present and recent past and so may seem to concentrate on the parties now in power, corruption is an aspect of the country's political culture, not the exclusive preserve of any particular group. For an attack on it to be effective, all political parties need to join in the effort, along with civil society and the international donor community. Corruption is emphatically not an issue that belongs to or should be misused for partisan political purposes, and it would be a major mistake to believe that a change of government after the September 2002 elections will automatically sweep away the problem.

RECOMMENDATIONS

To the Macedonian government and political parties:

1. Commit to fighting corruption as a major priority that extends beyond the life of the present government and the September 2002 elections and give concrete form to that commitment by accepting international proposals and strategies including those recommended below and those presented by civil society.

To the major international donors, including the European Union and its member states and the U.S., and international financial institutions:

2. Recognise the role of corruption in perpetuating instability in Macedonia and accept the need to play a leadership role in fighting it.
3. Develop programs and policy positions that deal with past corruption, not only preventing future episodes.
4. Identify as priority areas for corrective action those sectors that are especially susceptible to corruption because of the lucrative opportunities they offer or sensitive for the punishment and deterrence of corruption; in particular, urge the Macedonian government to agree to the appointment of international "watchdogs" to work inside the Health Insurance Fund, the Customs Service, the Prosecutor's Office and the Judiciary.
5. Condition financial aid to the government, in particular all balance of payments and budget support, on serious anti-corruption reform, and work with the government to develop realistic benchmarks to assess both good faith and effectiveness.
6. Make convictions and confiscations the express goals of a results-oriented anti-corruption strategy, as a complement to the existing approach that emphasises improving the "capacity" of Macedonian institutions and strengthening the legal framework.
7. Incorporate specific "follow-up" elements in all anti-corruption training programs.
8. Provide financial support for the newly formed governmental Anti-Corruption Commission so it can operate effectively as soon as it is launched in October 2002, and to Transparency International Macedonia's civil society effort to develop an anti-corruption strategy and build an "anti-corruption coalition".
9. Urge passage of legislation to limit the scope of parties when in power to make appointments on the basis of political patronage rather than competence.
10. Engage Albanian political parties and civil society more actively in the anti-corruption effort.

To the European Union (EU):

11. Appoint an EU Anti-Corruption Adviser in Macedonia to complement the work of the EU Special Envoy.

To the International Monetary Fund (IMF):

12. Relax restrictions on hiring additional personnel in the State Auditor's Office and related agencies.
13. Set targets of increased revenue for ministries where corruption is depleting revenue.

Skopje/Brussels, 14 August 2002



MACEDONIA'S PUBLIC SECRET: HOW CORRUPTION DRAGS THE COUNTRY DOWN

I. INTRODUCTION

Implementation of the Framework Agreement – signed at Ohrid on 13 August 2001 – remains the yardstick of Macedonia's progress from communal conflict to democratic stability. Important steps have been taken to fulfil key provisions of that agreement. Police redeployment to the “crisis areas” (formerly controlled by Albanian rebel forces) is complete, marred by few incidents and only occasional protests. Of those persons initially displaced by the conflict, 90 per cent are back in their homes.

On 7 March 2002, Parliament passed a broad Amnesty Law, ending for most former Albanian rebels the fear of arrest and trial as a “terrorist”. On 30 May 2002, a law was passed stipulating the use of Albanian language on identification cards, and on 20 June, fifteen other laws mandated by Ohrid were approved that reinforce language rights and give local communities a greater role in choosing police chiefs.

Attitudes to the international community have become less confrontational. Prime Minister Ljubco Georgievski proposed extension of the NATO mission's mandate, indicating that the alliance, long scapegoated by local politicians, has demonstrated its utility and even-handedness.

Yet the progress is fragile. International officials concede that the police “redeployment” plan is mostly cosmetic, mainly involving symbolic visits to Albanian villages. The former crisis regions still lack uniformed policing, leaving Macedonians especially

vulnerable in areas where they are a minority.¹ International sources increasingly acknowledge that infiltration is occurring, that stories about attacks on remote Macedonian security positions may have some validity and that some ex-NLA commanders retain both firepower and swagger.

Despite the impressive refugee return figures, UNHCR and ICRC acknowledge that Macedonian minorities still suffer from “low level harassment”, and the slow pace of house reconstruction and other infrastructure problems prevent some Albanians from returning home. Minority Albanians in the southern town of Bitola are said to be selling their property in response to incidents, as are ethnic minorities in other areas. Recent polling suggests that last year's conflict continues to weigh heavily on ethnic attitudes. Macedonians continue to resent the Ohrid concessions while Albanians complain that they see little practical change in their lives.²

A major component of the Ohrid Agreement – decentralisation of government – has hardly begun. Even the key instrument – the new Law on Local Self-Government – provides essentially just a framework that leaves critical details to be negotiated. The important companion bill – the Law

¹ UNHCR officials note that even the return of symbolic “mixed” patrols is misleading. In many villages, the “mixed” patrols lack Macedonian members, who fear for their personal safety. Interview with UNHCR on 8 August 2002.

² A U.S. State Department-sponsored poll conducted in May 2002 found that two-thirds of Macedonians oppose the Ohrid Agreement, while 90 per cent of Albanians support it. Three-quarters of Albanians believe that implementation is too slow. Office of Research, Opinion Analysis, Department of State, “Macedonian Public Questions Future of Framework Agreement: attitudes toward agreement provisions divide along ethnic lines”, 8 May 2002, pp. 1-2.

on Local Finance – will not be passed before fall, at roughly the same time the potentially contentious census is to be held.

Anything but self-sustaining, the Ohrid process has required constant tending by a trio of international mediators: U.S. Envoy James Holmes,³ in-country Ambassador Lawrence Butler, and EU Envoy Alain LeRoy. They have worked effectively together but even when they manage to surmount deadlocks over, say, the use of Albanian language on the cover of Macedonia's passport or the selection of election commission members, one of the parties frequently reneges, forcing further mediation.

The mediators' task has entered a new, even more complex phase with an election campaign that has not officially begun⁴ but has already produced worrying signs of more radical rhetoric.⁵ The likelihood is strong that both campaigns (the one in the Albanian community and the separate one in the Macedonian community) will play the nationalist card and further polarise the country.⁶

As Macedonia approaches parliamentary elections on 15 September 2002, opposition parties in both ethnic camps repeatedly express worry about election-related violence, intimidation and fraud – all prominent in past elections. Some senior

diplomats worry that the ruling Macedonian and Albanian parties could even collude to stage ethnic incidents or intimidate voters with a show of force. These concerns gain credence from the dubious record of the police,⁷ in particular the special unit known as the "Lions", under the command of Minister of Interior Ljube Boskovski.

Election-related spending has already complicated economic recovery. After Macedonia fulfilled the legislative prerequisites of the Ohrid Agreement, donors pledged more than a quarter billion U.S. dollars at a 12 March 2002 conference to finance reconstruction and reform but set as an explicit condition for the largest single component – U.S.\$165 million in balance of payments assistance – that Macedonia reach a standby arrangement with the IMF. Talks collapsed when the government refused to reduce election year spending commitments.⁸ As a result, donors have held back U.S.\$115 million intended to cover the payments gap.⁹

International experts say the economy has still not improved. Output is flat, unemployment alarmingly high in both communities, and ethnic Macedonians are emigrating in record numbers.¹⁰ Insiders say the government's reputation for corruption further inhibits the IMF from endorsing spending programs or loosening budget-deficit targets that could spur growth. In short, the government's own

³ On 11 July 2002, it was announced that Holmes ended his role. The indications from Washington are that he will not be replaced.

⁴ Elections are scheduled for 15 September 2002.

⁵ As an example, Democratic Party of Albanians (DPA) party leader Arben Xhaferi has declared himself a "radical" and adopted rhetoric to match. See "Xhaferi: We are the radicals"; *Fakti*, 10 June 2002: "When [Ahmeti's] ... party was formed I thought we were going to become a moderate party, but after their initial presentations, [Ahmeti's] party will take that position. Without any doubt we are the ones remained to continue our radical politics," said DPA President, Arbën Xhaferi in his speech to the rally in Tetovo on June 8." Ali Ahmeti, who otherwise seeks to rehabilitate his "terrorist" image, attempted to match Xhaferi with heavy use of Albanian imagery at his first appearance in Skopje since the conflict, when his party office, "Democratic Union for Integration", was opened on 30 June 2002. The Albanian anthem was played and homage was paid to fallen NLA fighters.

⁶ As ethnic Macedonians never cease pointing out, there are other ethnic groups in Macedonia besides the "big two". However, Turks, Serbs and others make up barely a tenth of the total population, according to the 1994 census. As in other parts of the Balkans, these small minorities have no territorial claims and, therefore, do not represent a primary source of conflict.

⁷ Among the most serious questions regarding police conduct is the 2 March 2002 slaying of seven suspected "Islamic terrorists". The Ministry has produced a book of "evidence" on the suspects, but journalists who have investigated claim they were probably hapless "economic refugees" in search of illegal entry to the European Union. See "Path to Europe Grows Perilous for Hopeful Muslim Refugees", *Wall Street Journal*, 28 May 2002, and "Macedonian Government Insists Ambushed Men Were Terrorists", *Wall Street Journal*, 4 June 2002. The international community has several times demanded that the "Lions" disband; see *inter alia* European Commission Staff Working Paper, Former Yugoslav Republic of Macedonia, Stabilisation and Association Report, Brussels, SEC (2002) 342, p.8.

⁸ The government approved a bailout for the "pyramid" savings bank TAT and accepted demands of state workers for a 10 per cent wage hike in the face of stern IMF warnings.

⁹ Information from banking experts in Skopje. Aid for reconstruction and implementation of the Ohrid agreement is unaffected by the failure of the IMF talks.

¹⁰ Data obtained by ICG suggest that applications to emigrate, which are chiefly from ethnic Macedonians, have doubled over the past year at some key embassies.

irresponsibility forces an austerity that may otherwise not be appropriate for a weak economy.

The credit crunch is another reason for the slack economy but the Central Bank keeps interest rates high, thus forcing borrowers into default and creating a disincentive for banks to lend money that entrepreneurs desperately require, because it also feels a need to guard against the government's election oriented profligacy.

In sum, the international community's most successful Balkan intervention is a relative and limited one. The ultimate goal of a stable and self-sustaining process permitting a diminished international profile remains elusive. The question is why?

The chasm between the two major ethnic communities is the most obvious explanation. But this merely states a fact – Albanian and Macedonian communities *are* divided. However, division does not explain why they nearly went to war in 2001. Nor does this perspective provide any solution other than a territorial division that would be as difficult to negotiate as to implement and would trigger a host of dangerous imponderables throughout the region.

Averting division and its inherent complications – not simply achieving nominal passage of Ohrid provisions – is the real international interest in Macedonia. Endemic corruption is a major contributing factor to the centrifugal forces still at work in Macedonia. The Ohrid bargain to diminish ethnic conflict by decentralising government institutions and boosting Albanian representation in them can only succeed to the extent the institutions function effectively and with credibility. In other words, a more egalitarian, less overtly ethnic state can only be realised if Albanians and Macedonians see the possibility to address grievances through the state.

However, instead of attenuating ethnic differences through shared government, Macedonia's ruling parties have functioned as corrupt coalitions, dividing turf among and within ministries and even on the ground for separate exploitation. The division of "turf" functions as a rehearsal for division of territory as politicians cynically present themselves as defenders of the national interest while in fact conspiring with the other side for personal or party enrichment. As bi-ethnic corruption has deepened, it has become more insidious – a racket in which

government inspection teams strong-arm businesses into "paying up". In turn, these rackets have created both means (ample cash) and motive (fear of judicial and political revenge) for ruling elites to influence the upcoming elections by intimidation or outright vote-buying.

Macedonians often complain, understandably, about vulnerability to trans-border insurrection from Kosovo. However, far less attention is paid to trafficking in contraband and weapons, not just by smugglers on mules but also by operatives cooperating with the authorities themselves.¹¹ Largely ignored is the critical link between corruption and smuggling – a pernicious development that has ramifications not only for the Western Balkans, but wider Europe as well. As one expert states, "corruption provides the oxygen for organized crime, and in many ways is the greater problem. It is difficult to address because it operates within legal frameworks, involving legal actors. It is easy to hold back those who are corrupt at the ground level, for instance, ... border guards ... but high level [corruption] is difficult to eradicate."¹²

The country's collective inheritance from the socialist era, its state and socially-owned enterprises, has often been privatised in a highly non-transparent manner. The end result is a weaker state with weaker borders and economy – a state that disappoints the law-abiding and creates extremists by angering those who feel that they have been denied their cut or had their principles abandoned for money. A senior government adviser

¹¹ Indeed, the very word, "smuggling", which connotes sneaking and concealing contraband from authorities, is often misapplied to Macedonia and possibly the region. Observers state that much of the "smuggling" is done in cooperation with or even by government officials, suggesting that a term like, "state trafficking", instead of the misleading "smuggling", would be more accurate. Terminology is more than an academic matter, since policy decisions flow from the perceived understanding of the problem. The Southeast Europe Cooperative Initiative (SECI), for example, operates on the basis that better cooperation among customs and police authorities will help stem the tide of "smuggling", even though an important component of the problem is the complicity of officials in both institutions.

¹² Dr. Paddy Rawlinson, Lecturer, Centre for Comparative Criminology & Criminal Justice, University of Wales, cited in "Improving European law enforcement and security co-operation to combat organized crime, corruption and illicit arms trafficking", report of seminar held 15-16 June 2001, Saferworld and EURISC Foundation, p.15.

states flatly, "corruption is the biggest threat to our national security".¹³

As cynicism and pessimism grow, especially among ethnic Macedonians, civil society weakens leaving corrupt officials more comfortable and brazen. As the cycle continues downward, the chances for conflict climb. Ohrid's new laws often seem irrelevant to unemployed Albanians and humiliating to dispirited Macedonians.

This report describes corruption in detail, showing how some of the scams work and what they mean for Macedonian stability. It also examines the international response to corruption, and how to improve it. It is not surprising that an international community that labours over the immediate Ohrid agenda has little zeal to confront the government on this most sensitive issue. However, the sad fact is that neither the EU, an individual important player like the U.S., nor any international organization is standing up and taking responsibility for fighting corruption.¹⁴ This leadership vacuum leaves the matter to institutions, associations and programs that generally assume good faith cooperation on the part of the authorities. For example, the GRECO-Council of Europe report on corruption in Macedonia will be based primarily on a questionnaire filled out by the government itself.¹⁵

The international approach to corruption is predicated on two fundamental misconceptions: that Macedonia's rulers actually have an interest in stemming the problem,¹⁶ and that Macedonia has

the time, as a normal country in transition, to follow a "long term plan." By showering aid on the government for fulfilling obligations to Albanians without demanding reform,¹⁷ donors inadvertently give the impression to many Macedonians that the Ohrid project itself is a kind of "pay off"; instead of looking generous and fair, the international community risks being pegged as one of Macedonia's "enablers."

There are two risks in highlighting the corruption issue now. The first is that it may diminish prospects for attracting critical foreign investment. However, as one senior Macedonian official engaged in the quest for financial stability said, "It is better to get the problem out in the open and fix it, than keep it in the dark".¹⁸ The second is that by releasing the report on the eve of an election campaign, ICG will be accused of having political motives. The report necessarily deals primarily with malfeasance of the government that presently bears responsibility for the country's affairs. Corruption did not first arrive in Macedonia with the current government, however, and some of the material presented below relates to politicians and parties currently in opposition but in power up to 1998. The record of that earlier period is a reminder that the upcoming elections are not likely to produce a panacea for the corruption problem regardless of the results. The best approach for any party interested in mitigating political fallout would be to consider the recommendations in this report, embrace civil society initiatives, and ask for more concerted international help.

The aim of this report is not to influence the election, but to ensure that the corruption issue and, more importantly, what can be done about it, reaches the broadest possible spectrum in Macedonia and the international community during the campaign. If anything is clear from efforts to achieve good governance in the Balkans, it is that simply holding elections and hoping "the next

¹³ ICG interview, 10 April 2002.

¹⁴ A few interested states like the Netherlands and the United States do fund programs, but officials describe them as aimed at preventing opportunities for corruption, not correcting abuses.

¹⁵ ICG interview with Stability Pact Anti-Corruption Initiative and Council of Europe staff members.

¹⁶ The remarks of Prime Minister Georgievski at an Open Society Institute conference on the subject, 21 June, 2002, suggest an attempt to shift responsibility for the problem: "We are facing the inevitable question as to whether corruption belongs exclusively to Macedonian citizens or whether Macedonia has been exposed to corruption from abroad". The prime minister insinuated there had been international corruption in the humanitarian response to the 1999 Kosovo refugee crisis. See "Our state has been exposed to corruption from abroad", *Nova Makedonija*, 22 June 2002. The Albanian DPA party has strongly protested ICG remarks on shared corruption in the country. DPA's parliamentary leader submitted a letter to this effect to ICG on 25 June while commenting orally at the same meeting that "we do not get as

much from corruption as you think", ICG interview with Zamir Dika, 25 June 2002. The independent magazine *Lobi* has written that the basic deal between DPA and VMRO-DPMNE is a one-third/two-thirds split. "Macedonia, one year on: Where are we going?", *Lobi*, 25 February 2002.

¹⁷ The cut-back in balance of payments funding was in response to the failure to come to terms on an IMF Stand-by Arrangement, not because of corruption *per se*.

¹⁸ ICG interview.

bunch will be more honest” is no solution.¹⁹ Both leading Macedonian parties have blemished records, as do two of the Albanian parties. Now is the time for Macedonia's citizens to ask not only who should lead the next government but *how* it can do better regardless of its party composition.

Precisely because the government is likely to be on the defensive, and because any future government will be less so, now is the best time for the international community to bring forward bold demands for reform and offers of assistance. Diplomats need not confront the government publicly on its record but they should present it privately with serious initiatives, for example, to insert international “watchdogs” in some of the institutions most susceptible to corruption. Whoever succeeds in the September 2002 poll will be bound by the commitments. Additional specific recommendations are detailed in the concluding section of the report.

II. ATTITUDES TOWARD CORRUPTION

The most extensive survey yet conducted of public attitudes across the Western Balkans showed that Macedonian and Albanian citizens of Macedonia are alienated in roughly equal measure from their political leaders.²⁰ They expressed the lowest level of public trust in their government (12 per cent),²¹ were most pessimistic about economic prospects, and had the lowest opinion of the truthfulness of local media in the region.

Respondents from both communities identified the most pressing problems facing the country as unemployment, poverty and corruption – three issues that straddle ethnic politics. Significantly, they worried about corruption in near equal percentages.²² Focus groups commissioned by the National Democratic Institute (NDI) expressed similar concern: “Both Macedonian and Albanians say that [among] the biggest problems facing the country are ... the lack of rule of law [and a] system [that] favours those with personal connections and political party affiliation”. Participants linked corruption to the poor state of the economy (the issue often cited as most important). An Albanian participant stated, “corruption is now the dominant force in our government. If we do not eliminate corruption, we will have more poverty”.²³

²⁰ The South East Europe Public Agenda Survey was conducted January-February 2002 by South East Europe Democracy Support) (SEEDS), commissioned by the International Institute for Democracy and Electoral Assistance (International IDEA). Full results are available at www.idea.int.

²¹ The second lowest level of trust was found in Serbia: 29 per cent.

²² Only three percentage points separated Macedonian and Albanian selection of corruption as a top issue of concern (41.7 per cent for Macedonians and 38.5 per cent for Albanians, according to the SEEDS survey, p. 5.) Other polls bear out the IDEA data, including one conducted in November 2001 by Transparency International which found that over 80 per cent said laws are not respected in Macedonia. A January 2002 poll by BRIMA-Skopje reported that 64 per cent of respondents believed increasing the competence of local government (as stipulated in the Ohrid Framework Agreement) would not reduce corruption.

²³ “Attitudes towards the Political, Social and Economic Conditions in Macedonia: Results of Focus Group Research”, Presented by Penn, Schoen & Bertland

¹⁹ The persistence of corruption and economic inefficiency in Croatia, despite a government that is demonstrably more transparent and honest, is testament to the need to rely on more than a change in parties and personalities.

Local experts repeatedly warn of the extent and perniciousness of corruption. Nikola Tupancevski, Macedonia's representative to the GRECO (Group of States against Corruption) initiative of the Council of Europe, recently stated that "Corruption threatens our state".²⁴ The Macedonian chapter of the non-governmental organisation, Transparency International, said that "Corruption has been accepted as a normal thing or way of life".²⁵ Gjorgje Marjanovic, professor of law at Skopje University and an opposition politician, claimed, with reference to corruption, that "Macedonia is not a state under law",²⁶ and "the Macedonian government is a totally irresponsible organism which must finally be put under guardianship".²⁷

Business surveys produce similar judgements. A 1999 World Bank study found that "[Macedonia] and Albania ... show higher levels of administrative corruption. These countries have extremely underdeveloped public administrations and lack control and accountability mechanisms within the state".²⁸ The "high cost of corruption" was second only to "state bureaucracy" as the main problem encountered in doing business, according to a survey by Transparency International, which found that four of ten investors in Macedonia had to bribe customs inspectors or officials to avoid interruptions in their work.²⁹

With varying degrees of conviction, international organisations and officials have also acknowledged that corruption in Macedonia is widespread. The European Commission's recent Stabilisation and Association Report states that "Corruption is a serious cause for concern.... Corruption in the public service is a widespread problem and undermines the

credibility of the political and administrative institutions".³⁰ The World Bank found that Macedonia is subject to especially high levels of "administrative corruption".³¹ Most recently, EU External Relations Commissioner Chris Patten said that "We are determined to see in [Macedonia] ... a really determined effort made to root out corruption. Corruption poisons political and economic life".³²

Most disturbing is that the trend in Macedonia – unlike most other Balkan countries – seems to be worsening. A survey commissioned by USAID found that five of seven indices measuring perceptions of corruption over the past year have declined. On the critical measure of "Involvement in Corrupt Practices", the survey notes that "the index values doubled."³³

Slagjana Taseva, Executive Director of Transparency International (TI) Macedonia, believes that as citizens have become aware of the extent of corruption, their tolerance has significantly decreased.³⁴ Disgust with corruption is fundamental to the lack of faith in institutions and politicians and presumably a major reason why so many say they will not vote this autumn.³⁵ However, abstention from the democratic process is more likely to encourage than challenge corruption.

Civil society organisations are too weak to mount an effective campaign against corruption. This can be done only by a new coalition of existing political groups or the international community. In practice,

Associates (Research commissioned by National Democratic Institute), 31 January 2002, pp. 4, 7.

²⁴ Interview in *Forum* magazine, 28 March 2002.

²⁵ *Forum* magazine, 28 March 2001.

²⁶ Interview with Professor Djordji Marjanovic, *Aktuel* magazine, 29 March 2002. Also, ICG interview with Marjanovic, 25 March 2002.

²⁷ *Dnevnik*, 22 April 2002.

²⁸ "1999 Business Environment and Enterprise Performance Survey (BEEPS)", commissioned by the World Bank and the European Bank for Reconstruction and Development, cited in the Stability Pact Anti-Corruption Initiative (SPAI) Steering Group report, "Anti-corruption measures in South-eastern Europe – Country reviews and priorities for reform", Council of Europe Press: Strasbourg, September 2001, p. 22.

²⁹ "Corruption and Foreign Investment cannot walk hand in hand", *Dnevnik*, 15 February 2002.

³⁰ European Commission Staff Working Paper, Former Yugoslav Republic of Macedonia, Stabilisation and Association Report, Brussels, SEC (2002) 342, p.3.

³¹ World Bank Study, cited in the Stability Pact Anti-Corruption Initiative (SPAI) Steering Group report, "Anti-corruption measures in South-eastern Europe – Country reviews and priorities for reform", Council of Europe Press: Strasbourg, September 2001, p. 22.

³² Speech by Chris Patten, EU External Relations Commissioner, to the Western Balkans Democracy Forum, Thessaloniki, 11 April 2002.

³³ "Corruption Indexes, Regional Corruption Monitoring", April 2002, USAID, Southeast European Legal Development Institute, in cooperation with Vitosha Research, p. 6.

³⁴ "The country is in crisis because of the corruption of government elites", *Kapital*, 10 January 2002.

³⁵ A poll commissioned in fall 2001 by the International Republican Institute (IRI) and leaked to local media found that almost half the respondents (47.1 per cent) either "didn't know" who they would vote for or did not favour any party mentioned. Few cited the separate category a "different party".

the latter is best placed to initiate such a campaign. This report examines the international community's reluctance to engage seriously with corruption and proposes how it might do so. First, however, to illustrate the scope of the problem and its implications for stability, it offers several case studies.

III. THE SPECTRUM OF CORRUPTION

A. FULL STATE CAPTURE: THE FREIGHT FORWARDER SCANDAL

The Stability Pact Anti-Corruption Initiative (SPAI) describes corruption as a symptom of poor governance and an impediment to the legal exercise of power through economic, social and political institutions.³⁶ The World Bank distinguishes between two major forms of corruption:

- “state capture” – meaning the ability of powerful individuals or firms to influence the formulation of laws or government policies to their own advantage.
- “administrative corruption” – when the implementation of laws and rules is influenced by bribes to public officials (e.g. to gain licences, remove customs obstructions, or win public procurement contracts).³⁷

A third, hybrid form now appears to flourish in Macedonia: *full* state capture together with administrative *coercion*. Not only are businesses prey to the demand for bribes; they are also subject to active reprisals and pressures if they do not give them.

The clearest alleged example is the Customs Service where, according to various sources, the Customs Director, Dragan Daravelski, is said to maintain a racket to coerce businessmen to use a favoured freight forwarding firm that is under his control. According to a customs official interviewed by ICG, use of rival shipping firms can result in “problems”.³⁸ This official, and another individual prominent in the freight forwarding industry, have

³⁶ Stability Pact Anti-Corruption Initiative (SPAI), Steering Group report, “Anti-corruption measures in South-eastern Europe – Country reviews and priorities for reform”, Council of Europe Press: Strasbourg, September 2001, p. 18. By contrast, organised crime has been defined as “groups who primarily focus on illegal gain, commit crimes with serious consequences for society and are able to screen these crimes in a relatively successful manner, in particular by showing that they are prepared to use physical violence or by ruling out persons by corrupt means.” Cited in Rawlinson, “The threat of organised crime”, op. cit., p. 13.

³⁷ “Anti-corruption in transition – contribution to the policy debate”, World Bank © 2000. See also SPAI Steering Group report, op. cit., p.19.

³⁸ ICG interview with customs official.

corroborated local press reports that assert Daravelski has eliminated or minimised the transport businesses that do not go along. It has been estimated that the favoured firm earns U.S.\$10,000 a day from the strong-arm scam. Allegations circulating publicly (some in the local press) include:

- Cigarettes for export to a Croatian firm were held up at the Tabanovce border crossing reportedly for failure to use the favoured firm. The Croatian government is said to have intervened in Skopje to try to get the goods moved.
- A competing freight firm, Fersped, claims in writing that 200,000 tons of cement product were blocked by customs and police officials in 2001 and 2002, "but when the job was undertaken by the [favoured] forwarder, the same transport was carried out normally and smoothly, and we lost the job due to obvious biased attitude of Customs authorities..."³⁹
- An importer of medical equipment with a contract for re-export stated that his trucks were blocked by customs officers until he dropped Fersped in favour of the favoured forwarder.⁴⁰

U.S. Ambassador Butler has publicly expressed disappointment with the Customs Service and called on business people to speak out about their problems: "Some goods are waiting at border crossings for a longer time [than necessary.] Some of our goods have been confiscated for no particular reason".⁴¹

³⁹ Text supplied to ICG: "Information on problems we have been facing with the Government officials of the Republic of Macedonia", Fersped A.D., Skopje, 12 April 2002. Fersped further alleges that consignments to KFOR in Kosovo have been held at the Greek-Macedonian border for more than 60 days, that the Customs House does not accept KFOR documents as certification of receipt of goods in Kosovo (thus, exempting from customs duties), and that the latter practice has resulted in unfair charges to it of €75,000.

⁴⁰ ICG interview.

⁴¹ "Butler: U.S. Government disappointed with Macedonian Customs", *Dnevnik*, 20 June 2002. Ambassador Butler is not alone in his disappointment; a shipment of several dozen copies of ICG Balkans Report 108, *After Milosevic: A Practical Agenda For Lasting Balkans Peace*, 26 April 2001, was held by customs officials for almost a year. A punitive "import tax" not envisaged in Macedonian legislation was demanded – for a publication that ICG wished to distribute

Customs Director Daravelski has insisted to ICG that neither he nor the Customs Service is involved in any of the alleged activities and that he has no relationship with any freight forwarder.⁴² It is, of course, appropriate that his denials be fully taken into account in any investigation. A strong public interest would certainly be served, however, by a thorough investigation by the appropriate Macedonian authorities, at the very least in order to restore public and business confidence.

1. Evolution of the problem

Corrupt links between large enterprises, state organs and political parties were a feature of the landscape in Macedonia long before the present government came to power. Corruption appears to have been widespread in, and under, the previous government, led by an SDSM-PDP coalition.⁴³ Fersped itself is alleged to have links to opposition parties and to have enjoyed advantages under the former government. Former Prime Minister Branko Crvenkovski, leader of the SDSM, once gave a memorable speech warning about the "octopus" of corruption but failed utterly to curb the problem.

However, the alleged freight-forwarding racket would demonstrate an important evolution:

- Instead of possible favouritism toward shipping firms with "connections" to the government (i.e. normal state capture), the new Customs racket appears to demonstrate *full* state capture: the fusion of private or party-owned or associated firms with elements of the state structure. As shown below, exploitation of state-sponsored rackets is reportedly not confined to freight forwarding.
- Instead of simple bribes for service ("administrative corruption"), the present allegations suggest systematic abuse of regulatory procedure to coerce usage of a favoured firm (administrative coercion).

In other words, senior elements of a state agency are believed to have evolved from passive opportunists

free of charge. ICG declined to pay, and the reports were never delivered.

⁴² ICG interview with Dragan Daravelski, 22 July 2002.

⁴³ Prominent examples given of alleged corruption are the failed "pyramid" bank, TAT, administrative corruption in Customs, procurement fraud, export fraud, alleged abuses in the car import firm Asiba, and non-transparent privatisation.

to active racketeers. As discussed below, there is a prospect of active smuggling collaboration between criminal elements and state structures. A prominent government minister conceded this evolution to ICG.

Pivara Skopje, Macedonia's leading brewery, has provided ICG written, detailed allegations of selective, arbitrary abuse of procedure by senior officials and former officials in Customs and the Public Revenue office.⁴⁴ Sources say that Pivara is harassed because it refuses to pay bribes. Other sources report similar patterns of corruption in other fields. One wealthy landowner claims two of his homes were bulldozed because he refused to pay a U.S.\$1 million bribe demanded by a government official.⁴⁵

Borce Davitkovski, a university professor of law, described the impact of administrative coercion as applied to a major pharmaceutical firm: "The Public Revenue Office ... inspected both the privatisation and the financial work and all the commissions found no irregularities. It is obvious that the intention is to create pressure. Such activities are not good for the economy ... or for foreign investment. Who wants to invest in a company that is under inspection every day?"⁴⁶

⁴⁴ Document provided to ICG by Pivara Skopje, AD, dated 10 April 2002. The allegations about Customs concern failure to permit a representative of the brewery to be present during the sampling of imported sugar, which ultimately triggered substantial tariffs, deliberate delay and refusal to provide Customs refunds. The allegations about the Public Revenue Office concern arbitrary and protracted revenue inspections as well as unauthorised confiscation of materials.

⁴⁵ Interview with ICG. The landowner provided documents to ICG.

⁴⁶ "Interview with Borce Davitkovski, professor at law faculty", *Aktuel* magazine, 5 April 2002. Professor Davitkovski has no official position with the SDSM but is believed to be close to that opposition party. The firm in question is the pharmaceutical house, Alkaloid. Alkaloid's Director claims that the firm already pays on average more than €10 million per year in liabilities to the state. "Investments in conditions of war and transition", Trajce Mukaetov, Ministry of Finance Bulletin, 12/2001, p. 97.

B. CORRUPTION AND THE OHRID AGREEMENT: THE HEALTH FUND SHAKEDOWN

With expenditures of almost U.S.\$160 million,⁴⁷ the Health Insurance Fund (HIF or Fund) essentially controls the national medical market. It functions as the payments mechanism for the state health system, procuring its medicine and equipment. The Director of the Health Fund, Vojo Mihajlovski, is also General Secretary of the ruling VMRO-DPMNE party.

The Fund has operated with a loss for years, mounting to U.S.\$37 million by 1998. To address this, firms that had signed contracts to supply drugs were asked to discount their terms (reduce what they were owed by the Fund) by as much as 25 per cent to get their accounts paid.

According to sources who claim first-hand knowledge, the procedure changed in mid-2000. Instead of being asked to reduce the amount owed, suppliers were reportedly asked to hand over 5 per cent of their accounts receivable in cash. This amount was deemed – in writing, according to a source – a contribution to the VMRO-DPMNE party. In other words, suppliers were required to rebate 5 per cent in cash directly to the party, instead of taking a 25 per cent reduction in the value of their tender. Many complied. This contribution was said to have then been raised to 10 per cent, and again to 15 per cent. One supplier says that the kickback is occasionally as much as 30 per cent. An observer attributes the hikes to the fact that "this is an election year". Sources say refusals result in the dispatch of inspectors, sometimes from the Public Revenue Office, to scour records for irregularities.⁴⁸

Sources also allege gross abuse in procurement of health care equipment, including what is said to have been a bribe amounting to U.S.\$425,000 for purchase of a cancer treatment device, and frequent purchases without tenders. The "contribution" is reportedly paid in cash and the "contributor" offered a receipt.

Officials at the State Audit Office confirmed to ICG that their examination of the Health Insurance Fund

⁴⁷ Ministry of Finance data, Bulletin 12/2001, p.22.

⁴⁸ ICG has interviewed individuals who assert that they experienced this.

in August 2001 found violations, *inter alia*, concerning procurement, use of assets, and tenders.⁴⁹ ICG has obtained a copy of the audit (which has not been made public). Besides assailing the overall accounting methods – “Health Fund financial reports are not prepared according to basic accounting principles” – auditors specifically found that:

- income for the fund was understated due to cancellation of obligations without the agreement of creditors and without a decision of the Administrative Board;⁵⁰
- there is no record of payments from the contributions from those insured; and
- a procurement contract was made by “direct agreement” with a firm that had not even bid on the tender when it was put out to the public.⁵¹

Monthly estimates for the revenue from the kickback scheme range from U.S.\$200,000 to \$250,000. Estimates of the total revenue from Health Insurance Fund corruption (including procurement fraud) range as high as U.S.\$20 million annually.

Financiers point out that in any system where kickbacks are as rife as they appear to be in the Health Fund, the natural adversarial relationship between buyer and seller (which normally produces the most economical price) is absent. Instead, the Fund shares the seller's interest in raising the price for drugs, since this will also boost the kickback.

Health Insurance Fund Director Mihajlovski did not reply to written ICG requests to discuss the above allegations.⁵² Since the operation of the health care system is of great concern to all citizens, however, it would serve a strong public interest for the Macedonian government to look carefully into and report on these matters. As a first step, the government should publish the report prepared by the State Audit Office.

⁴⁹ ICG interview with State Audit Office, 11 April 2002.

⁵⁰ Financial experts say that this is a reference to the kickback operation described above.

⁵¹ “Final Report for the Audit of the Annual Account for 2000 of the Health Fund”, State Audit Office, Republic of Macedonia.

⁵² ICG sought appointments with Mr. Mihajlovski, by letter and by telephone calls, on 15 July 2002 and 29 July 2002 without receiving a response.

1. Consequences

The alleged Health Insurance Fund shakedown would appear to have serious consequences for health care delivery and implementation of the Ohrid Agreement. In economic terms, kickbacks wrung from suppliers are a “saving” that should belong to citizens who contribute to the Fund. Ordinarily, any savings obtained from suppliers would be returned to the health care system to improve salaries of health care workers, reduce fees, upgrade conditions, or increase availability of care and medicine. Instead, a political party pockets the savings while the health care system deteriorates. Low wages encourage doctors and nurses to accept bribes for service.⁵³ Health care workers threatened to strike on 11 April 2002 over compensation.⁵⁴

Overall, as one expert stated, because true income and expenditure is never properly reported, the underlying poverty of the health system is never addressed because “new money” is always removed.⁵⁵

On 21 June 2002, at a corruption conference organised by the Open Society Institute, ICG questioned Prime Minister Georgievski about alleged corruption in the Health Fund. Without specifically addressing whether money has been diverted to the party, he stated that the Fund's deficit has been eradicated, and investment in health care has increased.⁵⁶

Authorities have recently acted against some relatively small fry. The police arrested one doctor (the Chief of the Psychiatric Department of the Military Hospital), accusing him of accepting bribes for declaring soldiers “mentally unfit for duty”.⁵⁷ The doctor, apparently one of several to be arrested for bribery, denies these charges and claims he was

⁵³ One source conveyed to ICG how a doctor working in the state system had insisted on a steep bribe (demanding more than was offered) for treatment; when the doctor moved to a better-paying private hospital, no such demand was made.

⁵⁴ “The Health Care Sector On Strike”, *Utrinski Vesnik*, 11 April 2002.

⁵⁵ Communication with health expert, 9 July 2002.

⁵⁶ Georgievski's response ignores the main point that, regardless of improvements in the balance sheet, kickbacks continue to drain funding away from the health system.

⁵⁷ “A corrupt doctor issuing false army release documents is arrested”, *Dnevnik*, 9 April 2002. The physician, Gjorgji Mitrovski, is accused of having accepted seventeen bribes in the amount of €1,500 each.

set up because his brother is close to President Trajkovski, who is at odds with the Prime Minister.⁵⁸ State controlled media report a crackdown on state pharmacies in Skopje and Bitola, leading to dismissal of the Director of the Bitola Medical Centre for the "illegal work of the pharmacy".⁵⁹ Such measures look too much like scapegoating, however, to increase public confidence in the system.⁶⁰

A central concept of Ohrid was to prevent Macedonia's disintegration by increasing Albanian rights and representation and decentralising government power. The Law on Local Self-Government was deemed so important that it was the sole bill formally stipulated as a prerequisite for the donors' conference to be held. Negotiations over the health sector were the most contentious element of the law.⁶¹ The Albanian parties reportedly demanded a third of the lucrative exploitation of the Health Insurance Fund. Having laboured for years to overhaul and privatise the health sector, donors persuaded the Albanians to accept instead accelerated privatisation of local clinics; decentralisation of limited aspects of the health care system, outside the Fund; and improved local oversight of the health care system, including of the Fund.⁶² Two innovations were contemplated: expansion of the Health Minister's existing "health council" to include more Albanians, and establishment of an independent, international "health watchdog".⁶³

Little has been done, however, to advance any of these measures. Privatisation remains mired; the health council has not been expanded; and the promised international "watchdog" has not been established. World Bank officials recognise the need for reforms but balk at financing the international watchdog, saying that officials will keep him in the dark then use the watchdog as an alibi against charges of corruption. They argue that the Macedonians themselves must "take ownership" of the situation through the Ombudsman and civil society initiatives, both of which the World Bank could support.⁶⁴

The Albanian DPA party – some of whose leaders are said to have fought hardest for the "one-third" share – is not among those vigorously demanding implementation of the deal for Health Fund oversight. On 28 February 2002, DPA members voted in parliament with their Macedonian coalition partners from VMRO-DPMNE to block a review of the above-mentioned state audit of the Health Fund.⁶⁵ In other words, instead of bringing facts about the suspected Fund malfeasance into the open, the DPA apparently helped cover for its coalition partner.⁶⁶ Having lost its alleged bid for a one-third share of Fund operations during the negotiations over the Law on Local Self-Government, DPA's interest appears to have reverted to managing its other "business arrangement" with VMRO-DPMNE.

As do their VMRO-DPMNE counterparts, DPA leaders chafe at accusations of corruption but while denying them one of their number has also said to ICG that "we do not get as much from corruption as

⁵⁸ "The Doctor in the Military Hospital is one of many that were to be arrested", *Utrinski Vesnik*, 10 April 2002.

⁵⁹ *Vecer*, 11 April 2002.

⁶⁰ "Corruption cannot be fought by eliminating the small fry", *Dnevnik*, 5 April 2002.

⁶¹ Two other issues emerged in the negotiations – over education and the right of municipalities to join administratively. Neither proved nearly as contentious as the squabble over the health sector.

⁶² Sub-paragraph (1)-9 of Article 22 of the Law on Local Self-Government sets out the specific competencies of municipalities over Healthcare: "governance of the network of public health organisations and primary care buildings to include representation of local government in all the boards of all publicly-owned health care organisations; health improvement; preventive activities; protection of health workers and protection at work; health oversight over the environment; oversight over contagious diseases; assistance to patients with special needs; and other areas that will be determined by law".

⁶³ These were agreed in so-called "side-deals" outside the formal terms of the law, according to EU sources.

⁶⁴ ICG interview with senior World Bank official in Skopje, 19 April 2002. Macedonian experts like Professor Marjanovic and former Justice Minister Vlado Kambovski believe that indigenous institutions and civil society are too weak to fight corruption unless they receive direct international assistance. Interview with Kambovski on 9 July 2002.

⁶⁵ According to Petar Gosev, leader of the opposition LDP, Nikola Popovski submitted a motion to parliament that the State Auditor's Report on the Health Fund activities should be discussed. The request was rejected by a majority in parliament on 28 February 2002. Only 23 MPs voted for the proposal.

⁶⁶ When asked why DPA effectively covered for VMRO-DPMNE and stopped debate of the Health Fund audit, a party official said only that, "parliamentary discussion serves no purpose". However, he added that, "everyone knows what is going on in the Health Fund" and maintained that DPA still wanted the appointment of the "watchdog". ICG interview with DPA parliamentary coordinator, Zamir Dika, 25 June 2002.

you think".⁶⁷ DPA's parliamentary leader did not explain why the party has not challenged published accusations from *Lobi* magazine editor Iso Rusi to the effect that the its main "achievement" had been to win VMRO-DPMNE agreement for DPA to take one-third of government spoils.⁶⁸

One DPA official, however, did allege that an SDSM member of parliament is closely involved with a pharmaceutical firm that frequently pays kick-backs to the Health Fund. A non-partisan pharmaceutical importer says that the firm wants to place the MP on its board of directors so that "if the opposition wins the election, they will already have a 'connection' to whomever is appointed the new Health Fund director".⁶⁹

The tendency for power-sharing under Ohrid to become a way to raise the Albanian share of government spoils is a major obstacle to realising the promise of the Law on Local Self-Government.

C. MULTIETHNIC CORRUPTION: "CONTINGENT" SALES IN A MINISTRY

A former deputy minister of economy in last year's "unity government"⁷⁰ has provided ICG what he insists is a striking example of the ease with which Albanians and Macedonians cooperate over corruption. Allegedly, in his first meeting with the (Albanian) head of his ministry, Besnik Fetai:

[Without my asking,] Fetai ... bluntly told me to speak to Inspector X⁷¹ and ask him to provide me with a list of the 50 biggest trade wholesalers. [He] told me to choose one of the wholesalers and send Inspector X there to "find irregularities". These irregularities would total about U.S.\$150,000 in penalties. He said that the seller would then be "encouraged" to offer about U.S.\$12-15,000 as a bribe to avert the penalties. [He] told me to keep the bribe, but to give about 20 per cent back to Inspector X.⁷²

The understanding reportedly was that the deputy would have liberal access to this shakedown, while staying off the minister's own "turf". Such a division of spoils by territory or sector is believed to be a common feature of the current coalition. Indeed, the former deputy minister describes his and the minister's mutual shock – his own upon receiving the offer, the minister's that it was refused.

Minister Fetai's real interest, according to the former deputy and others, concerned the practice of price-fixing and selling "contingents" (rights to import staples such as sugar, meat and cheese). This alleged scam rests on the legal right to restrict such imports to protect domestic producers from foreign competition. According to the former deputy, the ministry artificially raises prices by cutting off imports for a protracted period. A "contingent" of the item is then approved to an importer, and a fee is pocketed.⁷³ The former deputy minister estimated the take for officials selling contingents that he claimed to be aware of during his short tenure in office amounted to U.S.\$2.5 million, and that the total take over the same period was at least five times more.

In an interview this year, Minister Fetai downplayed his role in the selection of contingent awards:

In the Ministry of Economy there is a commission that has selected the companies

⁶⁷ Ibid. During the course of the meeting at which he made the quoted comment, Dika also handed over a letter denying in effect the accusations against the party.

⁶⁸ "Macedonia, one year on: Where are we going?", *Lobi*, 25 February 2002. Meeting with DPA parliamentary coordinator Zamir Dika, 25 June, 2002.

⁶⁹ ICG interview with pharmaceutical businessman, 12 July 2002. According to Transparency International Macedonia, the recently passed law on members of parliament would make such membership illegal.

⁷⁰ The former Deputy Minister is Zoran Vitanov of the Socialist party. The demand for an over-arching political settlement to the conflict made it necessary to broaden the DPA-VMRO-DPMNE government. The opposition PDP (Albanian) and SDSM (Macedonian) parties joined the government on 8 May 2001. Their national unity government lasted until late fall. The long-delayed constitutional amendments provided for in the Ohrid Agreement were passed on 16 November 2001, and SDSM left the coalition on 21 November.

⁷¹ The former deputy minister provided the name of the inspector to ICG.

⁷² ICG interview, 11 April 2002. The former deputy minister had said some of the same things publicly more than a half-year earlier. He is now a member of an opposition party. ICG has interviewed another source who reported the sale of contingents discussed below.

⁷³ Contingents are approved by a board on which several ministries are represented.

that have applied for sugar contingents and not me. About 50 companies have applied on the tender out of whom 30 are from the confectionary industry. The chairman of the commission, Imer Shabani, made the assessment and decided to grant the import to twelve companies. It was their decision and I only signed it. I don't know where the sugar was imported from, nor do I know the businessmen who imported the sugar.⁷⁴

This interview largely echoed the minister's assertion a year earlier that:

the decision of the government was to import white sugar for sale and not for production. Fifty companies have applied to the Ministry of Economy, twelve of whom are trade companies, and 38 are companies dealing with food products. According to the decision of the government and Article 24(a) of the Customs Law, that says if there is a lack of some product on the market that is important for the standard of living of the citizens, the Ministry of Economy has the right to intervene on the market. The decision was reached at one of the government sessions, after which the contingents were shared. The contingents are shared by the decision of the commission in the Ministry of Economy, and I only sign those decisions.⁷⁵

Zum magazine estimated the "price" for the rights to sell 15,000 tons of pork at U.S.\$ 12.5 million. It alleged that a single contingent sale to an official close to the minister cost U.S.\$200,000. The magazine also asserted that firms close to the ruling parties have had preferential treatment in relation to obtaining contingents, and that certain exporters of meat have advance notice of the sale of contingents and raise their prices accordingly.⁷⁶

Contingents should be awarded on the basis of proven merit (facilities, reliability, sanitary standards), or on a first-come/first-serve basis. They are alleged to go instead to those who can pay regardless of the size or requirement. For example, a

contingent for 1,000 tons of sugar was reportedly approved for a company with only three employees, while a company with over twenty supermarkets was granted only ten tons.⁷⁷ Other businessmen report similar allocations based on who is willing to "pay the price".⁷⁸ *Zum* estimates that the contingent sales practice costs the budget U.S.\$20 million. To put this in perspective, the recent U.S. pledge to assist Macedonia's balance of payments was U.S.\$16.5 million.⁷⁹

Such corruption allegedly has a double impact on the economy. It cheats the national bank of revenue, forcing taxes to be raised, and so further inhibits growth, and it makes consumers pay higher prices.

ICG has sought to provide Minister Fetai an opportunity to discuss the allegations that have been made about his actions. The Minister has not responded to ICG's request for a meeting.⁸⁰

Minister Fetai recently suggested in an address to Macedonia's American Chamber of Commerce that accession to the World Trade Organisation with the concomitant requirement to harmonise national law with international standards would help solve problems such as these because it would "increase transparency and reduce the opportunity for subjectivism in the treatment of businesses".⁸¹ In fact, the above instances appear to illustrate that often it is not the absence of laws that fosters corruption so much as the web of existing rules and regulations itself. According to Professor

⁷⁴ "Macedonian Economy suffers losses of DM 700 million from the crisis", *Vecer*, 10 April 2002.

⁷⁵ "Mega interview with Besnik Fetai", *Kapital*, 19 April 2001.

⁷⁶ "Albanian firms won the meat import", *Zum*, 20 April 2001.

⁷⁷ The Minister of Finance says that his ministry, which sits on the responsible board, did not approve these sales. ICG interview with Minister Gruevski, 16 April 2002. ICG reported allegations that the profit from a similar sugar deal involving 15,000 kilos of refined sugar in 2000/2001 was estimated at U.S.\$2.5 million. See ICG Balkans Report N°109, *The Macedonian Question: Reform or Rebellion*, 5 April 2001, p.13. The report cited a front-page *Dnevnik* article from 30 March 2001.

⁷⁸ Pivara Skopje, for example, has made public charges.

⁷⁹ U.S. data from Embassy Press Release, 12 March 2002.

⁸⁰ ICG submitted a request for a meeting to Minister Fetai at the beginning of April 2002 to which no response has been received. ICG subsequently spoke with Zamir Dika, a senior official of the minister's party, DPA, about the alleged activities both of Fetai and of the party generally. During the same interview, Dika submitted a letter to ICG contesting the allegations while commenting orally that "we do not get as much from corruption as you think". ICG interview with DPA parliamentary leader Zamir Dika, 25 June 2002.

⁸¹ U.S. Chamber of Commerce magazine, "Free Market Rules", February/March 2002, p. 8.

Davitkovski, Macedonia has “actually incited corruption by adopting regulations that gave huge discretionary rights to ministers ... If we prevent the possibilities for discretionary rights, then we will avoid corruption on the high level”.⁸²

The truly startling element of the alleged contingent sales scam is that it has been public for so long, with so little resonance. Press investigations were published more than a year ago, and the former deputy minister's allegations are almost as long in the public domain. Yet, typically, public charges have not been followed up by government action. At the very least the government should release all information at its disposal so that the public can make an informed judgement on the serious allegations.

The massive cynicism evidenced by citizens of all nationalities is produced by the combination of high public awareness of alleged corruption with equally high awareness that state institutions do not follow through on the allegations. This explains both Macedonia's low level of public faith in institutions, and the difficulty facing civil society leaders who want to mobilise the public against corruption.⁸³ Professor Marjanovic argues that power and invulnerability are natural partners in Macedonia: “People in power are untouchable; by definition, if you can be ‘touched’, then you are not a credible power”.⁸⁴ Taseva of Transparency Macedonia adds that corruption remains a “low risk, high reward activity”.⁸⁵

The near irrelevance of disclosure is not lost on Macedonia's politicians. Former Deputy Minister Vitanov says that he twice discussed the contingents scam with Prime Minister Georgievski, warning him of his intention to go public. “Go ahead”, the prime minister reportedly told him, “there is no such thing as ‘public opinion’ here”.⁸⁶

D. DEFYING INTERNATIONAL LENDERS: THE MAKEDONIA TELEKOM CASE

Corruption is by no means limited, however, to the actions of government officials. It pervades much of the climate of doing business in the country. The following case may illustrate how confident Macedonian business people are about engaging in questionable practices even when these are detectable by outside parties. According to international sources and Macedonians familiar with the transaction, the Macedonia Telekom Board declared itself two substantial dividends. The first dividend was declared on 30 November 2000, when the company was actively involved in privatisation. The second dividend was paid following the acceptance of the buyers' offer. The first dividend totalled between U.S.\$25 million and U.S.\$30 million and the second, which is in dispute, between approximately U.S.\$8 million and U.S.\$20 million.⁸⁷

Former Telekom officials insist that all dividends were fully disclosed to the buyers who ultimately paid €362.5 million for the company.⁸⁸ The buyers, however, say they were unaware of the second dividend and have challenged the amount of “sponsorships” (cash grants) given out by the Telekom management during and after the due diligence period.⁸⁹

Macedonian sources concede that the dividends violated loan covenants stipulated by the European Bank for Reconstruction and Development (EBRD). Indeed, they admit that the second dividend was declared after the EBRD had expressly warned the Telekom Board that it was acting in contravention of the loan terms.⁹⁰

This experience^{90A} is at least a cautionary tale for foreign investors, who may depend on the discipline that powerful international lenders like the EBRD might be expected to be able to impose on their

⁸² “Interview with Borce Davitkovski, Professor at Law Faculty”, *Aktuel* magazine, 5 April 2002.

⁸³ Such as the Transparency Macedonia executive director, Taseva, and its president, Zoran Jacev, and Open Society Institute (OSI) Macedonia Director Vladimir Milcin.

⁸⁴ ICG interview, 3 April 2002.

⁸⁵ This is why she campaigns for changes to laws and regulations to make confiscation of assets possible. For example, Transparency Macedonia urges that the tax rate for property whose origin cannot be established (set in the draft anti-corruption law) should be raised considerably.

⁸⁶ ICG interview, 11 April 2002.

⁸⁷ ICG interviews with a Macedonian insider, 12 July 2002, and with international sources, including on 12 August 2002, an individual associated with the purchasing consortium.

⁸⁸ ICG interview with a Macedonian insider, 12 July 2002.

⁸⁹ ICG interview with an individual associated with the purchasing consortium, 12 August 2002.

⁹⁰ ICG interview with a Macedonian insider, 12 July 2002.

^{90A} In a further development since this report was first published, former Makedonia Telekom CEO Daniel Doncev, in a strongly worded ‘Open Letter’ circulated to the Macedonian media on 9 September 2002, denied categorically that any undisclosed further dividend had been

borrowers.⁹¹ Yet, Macedonia can hardly afford to discourage investment. While figures vary depending on definitions, in a normal year Macedonia receives U.S.\$50 million to U.S.\$75 million in foreign investment. Excluding the one-off telecommunications sale (which produced €62.5 million), investment fell by 60 to 70 per cent in 2001⁹² and remains off in 2002.⁹³

The decline in foreign investment both raises the cost of capital for the local firm seeking to start up or expand and denies fuel to the economy as a whole. "No business project can pay off if it uses a loan that is to be returned with 20 per cent interest", says one private company.⁹⁴ High interest rates mean firms must use more revenue to service debt rather than in production and hiring. Overall demand drops, including for firms not dependent on foreign investment, and economic activity shrinks. Loss of foreign investors also means loss of foreign business and management techniques needed to build a stable economy.

Given the economic stakes involved, therefore, the Macedonian government should undertake an urgent review of its privatisation program to ensure that it operates pursuant to international standards and is deserving of investor confidence.

E. THE OKTA REFINERY PRIVATISATION

As in most transition countries, privatisation of state-owned property in Macedonia has often been anything but transparent, producing as a consequence concerns about whether purchase

paid. Whether or not Mr Doncev's account proves correct, it remains unchallenged that dividends were paid in breach of EBRD covenants and ICG's view remains that the whole transaction is one that would unquestionably benefit from high-level independent investigation.

⁹¹ There have been other cautionary tales, including some involving more than monetary dispute. Gideon Sandel, an Israeli citizen representing various businesses, claimed in writing to ICG that he was the subject of a spurious three-month detention in prison during the time of the previous (SDSM-led) government. He alleged that he was denied not only due process but also any subsequent acknowledgement of the basis for his arrest.

⁹² Interviews with IMF, and separately with the Small Enterprise Assistance Fund.

⁹³ Interview with IMF, 25 June 2002.

⁹⁴ "Expensive loans and corruption hamper development", *Capital*, 7 February 2002.

prices paid and other aspects of deals, including the behaviour of senior officials, were appropriate.

In some cases, purchasers are not after the physical assets themselves (which may be outdated and rusting socialist structures), but the monopoly and marketing rights that may go with the company. These rights were a major interest for Greek investors, Hellenic Petroleum and Meton-Etep,⁹⁵ during negotiations in 1998 and 1999 to obtain Macedonia's oil refinery, Okta. The deal resulted in Macedonia selling off at a price believed by objective analysts to be favourable to the purchasers not only a state asset, but virtually its ability to control the import and pricing of a strategic asset, oil. Much of Macedonia's energy sovereignty was effectively transferred to a firm from a neighbouring state with which Macedonia has a number of outstanding political issues.⁹⁶ International financial officials advise ICG that the U.S.\$32 million price did not represent fair market value and that the creation of a private monopoly was inadvisable. One independent investor with knowledge of the deal bluntly commented that it could only have been concluded "by an idiot or a corrupt official".⁹⁷

The path to the Okta deal was paved by passage in January 1999 of a new Law on Privatisation, which dropped the standard requirement that privatisations be put out for international tender in favour of a new policy permitting "direct negotiations" with the buyer. In this case, the government negotiated only

⁹⁵ Hellenic Petroleum and Meton-Etep purchased Okta through a holding company named EL.P.ET – Balkanike, Societe Anonyme Petroleum Trading and Investment. Meton-Etep is the firm that led construction of the recently-completed pipeline linking the Okta refinery to Thessaloniki, while Hellenic Petroleum is the primary oil marketer. The Greek government is the majority shareholder in Hellenic Petroleum. ICG interview with Petros Karalis, Managing Director of Okta and also of, EL.P.ET.Balkaniki, on 8 August 2002. ICG wrote to Hellenic Petroleum on 31 July 2002 requesting a meeting to discuss allegations concerning the Okta deal and to Meton-Etep on the same day for the same purpose. Hellenic Petroleum responded that Mr Karalis could speak for it. Meton-Etep did not respond. However, during the 8 August 2002 meeting cited above, Mr Karalis of Okta stated that he could speak for both Hellenic Petroleum and Meton-Etep on these matters.

⁹⁶ Political disputes resulted in Greece placing a near-total trade embargo on Macedonia from 1993 to 1995.

⁹⁷ For discussion of the Okta allegations, see *Start*, 28 May 1999, "Oil Strategy – A Trojan 'oil horse' of EL.P. ET. BALKAN?"

with Hellenic and so in effect locked out other potential bidders (for example, other major international oil companies).⁹⁸

The questionable direct negotiations practice attracted the attention of the World Bank, though only after the sale had been concluded. According to a senior Macedonian banker who said he had discussions with World Bank Director James Wolfensohn in the fall of 1999 (after the sale), the Bank wrote a letter to the government expressing its strong concerns about the transaction.⁹⁹ In the aftermath of the deal, the Bank imposed a requirement on Macedonia to adopt a new, transparent public tender method as an express condition for the disbursement of the second tranche of a major credit.¹⁰⁰

The Minister of Finance claims that both the IMF and World Bank recommended that Macedonia move toward "private sale". However, a senior World Bank official denies this and insists that international financial institutions have consistently pushed for public tenders.¹⁰¹

According to a copy of the Share Purchase and Concession Agreement concluded in May 1999 and obtained by ICG, the buyers of Okta promised to pay U.S.\$32 million over three years. In exchange, they obtained not only Okta's assets, but also the "exclusive right" to satisfy Macedonia's crude oil requirements through import for five years.¹⁰² Imports were to be virtually duty-free (at 1 per cent duty rather than what an Okta competitor asserts is

the normal 22 per cent).¹⁰³ The purchasers also acquired the right to set prices for oil (according to a formula) every two weeks. Okta received the right to calculate the overall quantity of oil necessary to satisfy Macedonia's energy requirements, using the refinery's own export performance as one criteria. Finally, the government remained liable for Okta's debts up to the date on which the deal was concluded.¹⁰⁴

Financial experts who have reviewed Okta's reports say the firm earned yearly profits in 2000 and 2001 of approximately U.S.\$5 million to U.S.\$6 million.¹⁰⁵ If so, that would mean the firm's profits over two years covered roughly one-third of the purchase price, presumably why a Macedonian magazine objected to the purchase price and wrote that "the Greek partner will buy Okta with money from Macedonian citizens".¹⁰⁶

Reportedly only U.S.\$15 million of the U.S.\$32 million purchase price has actually been paid. Finance Minister Gruevski confirms that the final tranche of the purchase price has not yet been paid, although he says that he expects this to be done soon.¹⁰⁷ Nearly one-third of the purchase price (U.S.\$10 million) is, under the terms of the agreement, to have been paid in as share capital for the pipeline linking the Skopje refinery to the Greek port of Thessaloniki, a project of one of the purchasers (Meton-Etep).¹⁰⁸

⁹⁸ Minister of Finance Nikola Gruevski affirms that the government only negotiated with Hellenic but maintains that this was because other potential buyers never followed through by demonstrating serious interest. ICG interview with Finance Minister Gruevski, 8 August 2002.

⁹⁹ ICG interview with senior Macedonian financial official, 29 July 2002.

¹⁰⁰ The second tranche of the FESAL (Financial and Enterprise Sector Adjustment Loan) amounted to U.S.\$30 million. See World Bank Report N°P 7935 MK, 17 November 2000.

¹⁰¹ Separate ICG interviews on 8 August 2002 with Finance Minister Gruevski and (by telephone) World Bank Country Director Marie-Helene Bricknell. Gruevski has provided a copy of a letter to the IMF Managing Director from the Director of the Central Bank dated 1 June 1998 indicating government policy to offer direct sale of state assets. Gruevski wrote a letter to Bricknell on 12 May 2000 promising that the law permitting sale of state capital through direct agreement would be abolished.

¹⁰² Share Purchase and Concession Agreement, Article 5.

¹⁰³ Ibid, Article 8, states that the purchaser will pay not more than 1 per cent duty. Makpetrol, Okta's competitor, has asserted to ICG that the normal duty is 22 per cent. Makpetrol and Okta confirm that they have reached an understanding under which Makpetrol will purchase oil products from Okta. ICG telephone interview with Makpetrol Director, 8 August 2002, and separate meeting with Karalis of Okta also on 8 August 2002.

¹⁰⁴ Ibid, Article 6, sets out the assumption of the company's liabilities and provides that "Vendor shall undertake and assume on the date of Closing fully, irrevocably and definitively all of Company's Liabilities as relate to the period up to and including the date of closing ..."

¹⁰⁵ Okta's Managing Director says the annual profit is about U.S.\$4 million. ICG interview with Petros Karalis, Managing Director of Okta and also of El.P.ET.Balkaniki, on 8 August 2002.

¹⁰⁶ *Start*, 28 May 1999.

¹⁰⁷ ICG interview with Finance Minister Gruevski, 8 August 2002.

¹⁰⁸ Share purchase agreement, paragraph 4.1(d). As a consequence, the purchasers of Okta are believed to enjoy now the exclusive right to supply Macedonia by oil pipeline

Okta's buyers insist that they have "lost money" on the deal, due to the sizeable investments they have made in infrastructure.¹⁰⁹ Okta and the government maintain that the deal was beneficial to Macedonia as it preserved 1,200 jobs. When questioned about the deal, Prime Minister Georgievski frequently says that Okta was a loss-making and rusting enterprise.¹¹⁰

The terms of the Okta deal contemplate that the firm's preferential duty position might be ruled unconstitutional; in that event, the agreement imposes an obligation on the government to levy taxes to ensure that Okta maintains its pre-eminent position.¹¹¹ Okta's main competitor, Makpetrol, has a challenge before the Constitutional Court, claiming that Okta's import monopoly is both unconstitutional and inconsistent with the (free trade) Stabilisation and Association Agreement (SAA) that Macedonia subsequently signed (in April 2001) with the European Union.¹¹²

The full terms, including the "Share Purchase and Concession Agreement", have not been made

for twenty years. This would, contractually, seem to block the competing "AMBO" (Albania – Macedonia – Bulgaria) project that some analysts believe would add an important, stabilising east-west balance to regional development. See "Building an interest-based relationship between Macedonia and the U.S.", remarks presented by Glenn Levine, Adjunct Fellow at the Center for Strategic and International Studies, Washington, DC, at the Process 2002 Roundtable on Macedonian National Security, 11 May 2002.

¹⁰⁹ ICG interview with Petros Karalis, Managing Director of Okta and also of El.P.ET.Balkaniki, on 8 August 2002.

¹¹⁰ ICG questioned the Prime Minister about the Okta deal and other corruption issues at a public forum sponsored by the Open Society Institute on 21 June 2002.

¹¹¹ Share Purchase Agreement, Article 8.

¹¹² ICG interview with Makpetrol President Josifovski, 12 April 2002. Makpetrol cites paragraph 33 of the SAA. Makpetrol document, paragraphs 7.2 and 7.3.3. The SAA mandates abolishment or progressive reduction of duties for all importers, not just selected firms. See SAA, Title IV "Free Movement of Goods", Chapter I "Industrial Products", Article 18. Makpetrol document, paragraph 7.3.2.1. Although Makpetrol and Okta have come to agreement on purchase of Okta oil products, Makpetrol officials insist that this has no bearing on the case before the Constitutional Court. ICG telephone interview with Makpetrol Director, 8 August 2002. Okta counters that that the government is in breach of the contract by permitting rival Makpetrol to import oil, contrary to the monopoly position enjoyed by Okta. ICG interview with Petros Karalis, Managing Director of Okta and also of El.P.ET.Balkaniki, on 8 August 2002.

public,¹¹³ helping to fuel widespread concern that senior Macedonian officials may have received handsome "commissions" as part of the deal. One politician has estimated these at U.S.\$5 million; another estimate alleged that between U.S.\$5 and U.S.\$15 million ended up in private accounts.¹¹⁴ Asked directly by ICG whether a commission had been paid in connection with the Okta sale, the managing director of Okta, who indicated that he could speak also on behalf of Hellenic and Meton-Etep, stated that he "did not believe that such money was paid".¹¹⁵

The scope of the Okta deal and the implications of the allegations surrounding it are of such a magnitude that the Macedonian public has a clear interest and right to examine the full record of what was done on its behalf by its elected representatives. The Macedonian government should produce the full record so that the public can make up its own mind based on all available documentation.

F. INSIDER DEAL MAKING: MAKEDONSKA BANKA

While corruption in Macedonia is often brazen, occasionally there arises the need to find "fronts" to cover for the true ownership interest. The media have identified a number of such cases, perhaps the most prominent of which involves the transfer of ownership with respect to a major bank, "Makedonska Banka".

Following a series of major acquisitions by the VMRO-DPMNE party, the Constitutional Court in 2001 struck down a provision in the law on political party financing that had appeared to permit such holdings.¹¹⁶ The Constitutional Court made clear that it was concerned that political parties not engage in for-profit trading activities. Instead of cleanly divesting itself following this ruling, VMRO-DPMNE allegedly placed the shares of Makedonska Banka in which it held substantial

¹¹³ Makpetrol document, paragraph 4.

¹¹⁴ "Macedonian Corruption Stories", *Alternativna Informativna Mreza (AIM)*, 30 April 2001.

¹¹⁵ ICG interview with Petros Karalis, 8 August 2002. Mr. Karalis is managing director of both Okta and El.P.ET. Balkaniki.

¹¹⁶ Decision of the Constitutional Court published in Issue Number 70/92 of the Official Gazette of the Republic of Macedonia. See also, "The constitutional court closes the party companies", *Dnevnik*, 1 March 2001.

interests in the hands of three “party soldiers” – the so-called “bachelors”: Electric Utility (ECM) Director Lambe Arnaudov, Health Insurance Fund Director and General Secretary of VMRO-DPMNE Vojo Mihajlovski, and Marjanco Koneski, a driver by profession.¹¹⁷ According to banking officials, the “bachelors” have recently transferred their shares to an individual whose background and identity are not fully clear.¹¹⁸

Central Bank and World Bank officials have confirmed that the stock transfers were made to “the bachelors”.¹¹⁹ The former fault the World Bank for inadvertently making these transfers possible by having insisted on a change to legislation that denied the Central Bank the ability to challenge acquisitions of less than 10 per cent of total capitalisation. They say that VMRO-DPMNE was able to exploit this by making the transfers to the bachelors in transactions each of which was just under the threshold that would have required Central Bank approval.¹²⁰ The independent daily, *Dnevnik*, identified the precise stock-exchange transactions as follows: the printing firm Goce Delcev, widely known to be controlled by VMRO-DPMNE,¹²¹ sold its nearly 10 per cent of the shares in Makedonska Banka to driver Koneski allegedly at far below their value; Arnaudov allegedly obtained the same amount of shares for the same price; and Mihajlovski picked up 8 per cent of the total shares from three different firms.¹²² Mr. Mihajlovski did not respond to written ICG requests to discuss these matters.¹²³

In a major interview Prime Minister Georgievski was asked how a driver could become a co-owner of a bank. Georgievski did not deny the allegation but replied that after “the Constitutional Court [ruling],

... VMRO-DPMNE decided to grant all its shares that it has in some companies to its members, or to sell those stocks to party members for legal prices”. The prime minister thus appeared to acknowledge that the purpose of the transactions was specifically to keep the capital effectively within the party’s control, that is, to circumvent the express purpose of the Constitutional Court ruling. To the journal’s follow-up question, “What if those receiving the stocks eventually dissociate from the party?”, Georgievski answered: “We believe they will not. We are talking about trusted people in our party”.¹²⁴

Makedonska Banka is not just another bargain-basement acquisition. According to a senior Central Bank official, one purpose to which the bank is put is to funnel capital to other firms that have been acquired by the party and then transferred in similar sham transactions to “party soldiers”.¹²⁵ Control of a bank provides its owners with information about the financial position of depositors or borrowers, which is a resource that potentially can be used to influence their actions. Having a bank within party control also means that funds – whatever their source – can move in and out of the country with little risk of detection.

The transfer of shares to trustworthy party members may have stayed within the formal letter of the law (and indeed it is possible that following further transactions VMRO may no longer effectively control the bank), but the affair appears at the least to raise significant questions of political ethics. It would be useful for the individuals and organisations concerned to lay out the full details in order to enable Macedonian citizens to make informed judgements about the proprieties.

While acquiring outright a *private* bank, the party also moved to ensure that it would maintain political influence in a *public* bank – the Macedonian Development Bank. In February 2002, the government engineered the firing of Vladimir Naumovski, the respected director of the Macedonian Bank for Development Promotion. Diplomats believe the real reason why Naumovski was fired is that he resisted pressure to authorise questionable loans to government cronies and that with his bank already designated to oversee donor

¹¹⁷ VMRO-DPMNE is believed to have acted similarly with other institutions in which it held major interests but the Makedonska Banka case is the most notorious. ICG interviews with banking officials, 21 and 25 June 2002.

¹¹⁸ ICG interviews with banking officials, 21 and 25 June 2002.

¹¹⁹ Ibid.

¹²⁰ Ibid.

¹²¹ See, for example, “Strike in Printing Firm ‘Goce Delchev’”, *Utrinski Vesnik*, 9 August 2002: “The printing firm is owned by VMRO-DPMNE”.

¹²² “VMRO-DPMNE increases its bank capital”, *Dnevnik*, 20 June 2001.

¹²³ ICG sought appointments with Mr. Mihajlovski, by letter and by telephone calls, on 15 July 2002 and 29 July 2002 without receiving a response.

¹²⁴ Interview with Prime Minister Ljubco Georgievski, *Dnevnik*, 31 December 2001.

¹²⁵ ICG interview with senior Central Bank official on 25 June 2002.

funds for Small and Medium Enterprise (SME) support, he may have presented an obstacle that had to be removed.¹²⁶

Finance Minister Gruevski denies that the firing was for this reason, implying instead that Naumovski's own questionable dealings led to the dismissal.¹²⁷ Naumovski's replacement, Dragan Martinovski, not only suggested that Naumovski was corrupt but also said the ex-director was responsible for the Development Bank having a "non-performing portfolio" of almost 70 per cent.¹²⁸ Although he alleges poor performance under Naumovski's leadership, Martinovski acknowledges that, unlike Naumovski, he himself has no experience managing a bank portfolio of any kind.

G. PRESSURE ON THE COURTS: THE MAK TABAK TAKE-OVER

The tobacco firm, Makedonija Tabak 2000, is managed by Stevco Kocevski, who is related to Prime Minister Georgievski's wife, Snezana.¹²⁹ Installing a family member appears to have been a priority for the prime minister's party in order to take over the firm. According to stockholders and former board members, pressure was brought in September 1999 on the former president of Makedonija Tabak, Straso Nelovski, a member of the Social Democrat party, to resign. Once Kocevski took his place, eight other members of the

former board were pushed out.¹³⁰ In December 1999, the revamped board took a decision to create a new company, Makedonija Tabak 2000.¹³¹ Over the next six months, the predecessor company, Makedonija Tabak, declared bankruptcy, and an administrator was handpicked to oversee its affairs.

According to stockholders and others claiming familiarity with the case, the bankruptcy administrator permitted all assets to go to the newly-formed "Mak Tabak 2000" company, while the liabilities, allegedly amounting to nearly U.S.\$25 million, remained with the predecessor.¹³² Then, in a financial sleight-of-hand, "Mak Tabak 2000", through its stake in another company ("Gold Mak"), become the largest shareholder in Tutunski Kombinat – a company to which Makedonija Tabak owed at least four million Euros. In other words, a putsch against the former board of Makedonija Tabak resulted in formation of a wholly new shell that absorbed not only all its assets – while leaving its liabilities behind – but also one of its major creditors.

Stockholders and former board members of Makedonija Tabak filed suit in a Skopje court in June 2001 demanding the "erasure" of the official registration of Makedonija Tabak 2000 and that the court enjoin the company from disposing of any assets.¹³³ In August 2001, the court issued an order effectively freezing the company's assets pending a final decision on stockholders' rights. Stockholders assert that Makedonija Tabak 2000 ignored the court's order and sold off property while appealing. In December 2001, the appeals court upheld the lower court's decision. In April 2002, stockholders

¹²⁶ Far from being an obscure example in an obscure sector, economists look to the growth of SMEs to stem Macedonia's massive unemployment, estimated by the State Statistical Office at between 30 and 40 per cent while almost a quarter of those with jobs do not receive regular wages.

¹²⁷ ICG interview with Finance Minister Gruevski, 16 April 2002.

¹²⁸ ICG interview with Macedonia Development Bank Director, Dragan Martinovski, 22 April 2002. Naumovski denied the allegations and maintained that he has documents to rebut them. Further, he claimed that nowhere on his dismissal notice is there any mention of wrongdoing. ICG interview with Vlado Naumovski, 26 April 2002. The Finance Minister told ICG that wrongdoing was not cited as an official reason for dismissal because the government would have been forced to go to court and "it lacked proof". ICG interview with Gruevski, 16 April 2002.

¹²⁹ Kocevski's sister, Vesna Takovska, is married to Snezana's brother. Mrs. Takovska is the director of Tabak Osiguruvanje (Tobacco Insurance Company), a firm that grew out of the original Makedonija Tabak enterprise.

¹³⁰ According to the lawyer for shareholders in Makedonija Tabak, at the time Mr Kocevski became managing director, the firm's capital belonged 63 per cent to shareholders and 37 per cent to the Privatisation Agency. ICG telephone interview with Sasha Krstich, 12 August 2002.

¹³¹ Makedonija Tabak 2000 was formally registered in February 2000, although the decision to create it was taken two months earlier, even before its predecessor had been declared bankrupt. Stockholders insist that Makedonija Tabak was not bankrupt. ICG interview with former board members and stockholders of Makedonija Tabak, 2 July 2002.

¹³² ICG interviews.

¹³³ Stockholders have also filed a separate suit asking the court to affirm that they are the rightful owners of the company. Stockholders showed ICG a letter from the Minister of Finance discouraging this claim, and a separate document from the Registry Office purporting to endorse it. ICG interview with stockholders, 3 July 2002.

further assert, Makedonija Tabak 2000 moved its headquarters from Skopje to Stip to complicate disposition of the case and seek more favourable judges. The Skopje court must now rely on the Stip court for certain aspects, and the latter body, stockholders claim, is friendly to Makedonija Tabak 2000.¹³⁴

Mr. Kocevski, the director of Makedonija Tabak 2000, has denied the shareholder allegations to ICG and stated his view that “the court process is finished”. Shown internal documents concerning the take-over and transformation of Makedonija Tabak, Kocevski did not challenge their authenticity but said they contained nothing improper. He said that the key decisions in this regard were taken by a “council of those people who had assets” and described the process of takeover and transformation into Makedonija Tabak 2000 as having a “special history”. He explained the formal move of the company to Stip as caused by the fact that the firm did not own the building’s sizeable modern quarters in Skopje (where the meeting with ICG took place).¹³⁵

Stockholders bringing the Makedonija Tabak case tell ICG they believe that the judges hearing their case are not so much corrupt as intimidated. Neda Zdraveva, Law Program Coordinator for the Open Society Institute in Macedonia, says that political interference in the judiciary is a chronic problem and that senior politicians have sought to influence the selection of judges in cases in which they have an interest.¹³⁶

In an apparent recent example of the quest to wield political influence over the judiciary, a senior VMRO-DPMNE politician, the vice president of the parliament, Tomislav Stojanovski, whose son is Customs Director Dragan Daravelski, was appointed to a seven-year term as a member of the Judiciary Council (the supposedly independent commission that selects nominees for the bench and otherwise supervises the “competence and ethics of judges in the performance of their office”¹³⁷) on 18 July 2002.¹³⁸ This appointment appears to be in

direct conflict with the constitution, which forbids the members of that council to hold other public office or be active in a political party.¹³⁹

Zdraveva notes that polls show that the public perceives corruption in the judiciary to be high. While the courts are certainly not free from corruption, however, the efforts of Makedonija Tabak 2000 to change venue suggest that some judges are resistant to pressure or inducement. The Constitutional Court on the whole seems to show a remarkable degree of independence.

The implication that the judiciary suffers more from vulnerability to political influence rather than pure corruption is important. Insulating judges from political pressure is more achievable than would be rooting out endemic corruption on the bench itself.

H. STATE TRAFFICKING: THE TOBACCO TRADE

The tobacco industry is a vital element of Macedonia’s economy, engaging 16 per cent of the population.¹⁴⁰ It has long had links to the government and to politics. Before the arrival of Kocevski and his team with ties to the present government, the business was dominated by the legendary Danco Suturkov, who was close to the former SDSM government and for many years was known as the tobacco baron of Yugoslavia.

However, tobacco has historically had a darker side in Macedonia as well. Tobacco smuggling is “natural” to the country in two ways: first, by its geographic position as a Balkans crossroads linking with Greece, Bulgaria, southern Serbia and Kosovo, and Albania; secondly, as a significant producer (the world’s seventh largest) of high-quality Oriental (aromatic) tobaccos. Former Interior Minister Pavle Trajanov, the magazine *Fokus*, and others have alleged that Customs Director Dragan Daravelski is the mastermind of present day tobacco smuggling in

¹³⁴ Ibid.

¹³⁵ ICG Interview with Stevco Kocevski, 8 July 2002.

¹³⁶ ICG telephone interview with Neda Zdraveva, 3 July 2002.

¹³⁷ Macedonia’s Constitution, Article 105.

¹³⁸ “Tomislav Stojanovski appointed a member of the Republic Judiciary Council”, *Dnevnik*, 18 July 2002.

¹³⁹ See Macedonia’s Constitution, Article 104 (5): “The office of a member of the Republican Judiciary Council is incompatible with the performance of other public offices, professions or membership in political parties”. Also, in a similar vein, Law on the Republic Judiciary Council, Articles 5 and 7.

¹⁴⁰ Stevo Kocevski, Director of Makedonija Tabak 2000, “Some observations on the conditions in the world tobacco production and in our country”, Ministry of Finance Bulletin, 12/2001, p. 100.

Macedonia and that he enjoys full government backing at the highest level.¹⁴¹ The further allegation is widely-made that Tutunski Kombinat in Daravelski's hometown of Kumanovo, which manufactures many of the most popular brands of cigarettes and has been acquired by Makedonija Tabak 2000, is a centre for counterfeit cigarette production.¹⁴²

Customs Director Daravelski flatly denies any involvement in illicit tobacco trafficking and states that there is no illicit production of cigarettes in Macedonia.¹⁴³ Nevertheless, there are unusual circumstances that appear to warrant close investigation, in the public interest, by the appropriate Macedonian authorities. ICG has obtained a document of Tutunski Kombinat Kumanovo in which the company affirms that it produces the "Assos" brand cigarette. The owner of the "Assos" brand insists to ICG that it has never had an agreement with any Macedonian company for the production of its cigarettes.¹⁴⁴ ICG has also obtained production logs purportedly from Tutunski Kombinat Kumanovo that appear to record the production of a number of brands of cigarettes, including the "Monte Carlo" brand, now owned by Japan Tobacco. This company has recently written a sharp letter to the prime minister of neighbouring Serbia complaining about a "massive counterfeit

and smuggling scheme" involving the Monte Carlo brand in Yugoslavia.¹⁴⁵

Daravelski is also alleged to use the same methods to remove or limit competition in the tobacco industry as he has been accused of employing with respect to freight forwarding. For example, a Slovenian firm, Tobacna, is said to have purchased the Skopje tobacco factory TKS at what seemed a favourable price, until, a Customs official told ICG, its product was blocked by Customs in order to extort a U.S.\$1.5 million bribe.¹⁴⁶ Mr Daravelski firmly denied such allegations to ICG.¹⁴⁷

Prime Minister Georgievski indirectly acknowledged there is a problem with tobacco when he expressed the need to eliminate excise taxes on cigarettes that provide an incentive for smuggling.¹⁴⁸ The media and the Finance Minister have long spoken of the existence of serious improprieties in Customs.¹⁴⁹ Public Prosecutor Djikov, a political appointee of VMRO-DPMNE, confirmed to ICG his concern about customs operations.¹⁵⁰

Big money can be made by moving cigarettes, whether licensed product or illicitly produced counterfeits, to markets in both Western and Eastern Europe.¹⁵¹ One estimate puts the value of a single truckload of illicit cigarettes at nearly U.S.\$100,000

¹⁴¹ In spring 2001, *Fokus* ran a detailed, three-part series on what it described as Daravelski's smuggling operation, citing names, addresses, quantities and methods. ICG has interviewed separately the author of the *Fokus* series and other sources who back up the allegations in that publication.

¹⁴² See, for example, the above cited three-part series in *Fokus*, spring 2001.

¹⁴³ ICG interview with Customs Director Daravelski, 22 July 2002. While Daravelski denied that there was any production of counterfeit cigarettes in Macedonia, and insisted that such issues were outside the realm of the Customs Administration, he handed over an official Customs magazine, *Carinik*, which carries a story about an alleged illegal Marlboro cigarette factory in Kosovo. Daravelski, like Finance Minister Gruevski, stated that Kosovo was "the generator of crime and corruption in the region". See *Carinik*, Number 9, 5 July 2002, "Marlboro made in Gnjilane [Kosovo]". According to the Custom Administration's annual report (p. 20), only six criminal cases were brought in 2001.

¹⁴⁴ The document is "Decision" of Tutunski Kombinat Kumanovo dated 1 November 1999. The owner of the "Assos" brand is the Papastratos Cigarette Company of Athens, Greece. ICG interview with Export Director Arvanidis of Papastratos, 31 July 2002.

¹⁴⁵ "This week a four-eyes meeting of Japan Tobacco and Zoran Djindjic", *Svedok*, 23 July 2002, p.3.

¹⁴⁶ ICG interview with Customs official. For the discussion of freight forwarding issues, see chapter III A above.

¹⁴⁷ ICG interview with Customs Director Daravelski, 22 July 2002.

¹⁴⁸ Prime Minister Georgievski to the Open Society Institute's conference on corruption, *Nova Makedonija*, 22 June 2002.

¹⁴⁹ "Customs ... is still one of the weakest points of the institutions in the system": in "Crime, grey economy and corruption", Finance Minister Nikola Gruevski, 31 March 2002. Gruevski elaborated on his views when interviewed by ICG on 16 April 2002.

¹⁵⁰ ICG interview with Public Prosecutor Stavre Djikov, 25 April 2002.

¹⁵¹ Eastern Europe is known to be a market especially for counterfeits. The EU recently pursued and lost a lawsuit in which it claimed that U.S. tobacco giants Phillip Morris and R.J. Reynolds intentionally oversupplied countries in Eastern Europe so that the surplus would be smuggled into the EU, costing billions in lost taxes. "Judge throws out EU suit against tobacco companies", Associated Press, 20 February 2002. The Danish press has aired the question whether that country's largest cigarette producer, ST, may have exported cigarettes to supply smugglers "in countries such as Macedonia". *Politiken*, 13 February 2002.

(allegedly with customs officials normally getting a percentage).

Trafficking in illicit tobacco is a form of organised crime. Unlike organised crime in the West, however, criminal networks in the Western Balkans often work through state institutions, not around them. All too many officials of customs and state security services in the region (both secret and uniformed) are reputed to collaborate actively in smuggling. In this sense, "state trafficking" or "state-assisted trafficking" may often be a more accurate term than "smuggling".

Moreover, although cigarettes are a safer and simpler commodity to traffic than drugs, women or weapons, the activities are closely linked and interchangeable. A recent study of organized crime, corruption and illicit arms trafficking states that increasing trafficking in drugs, people and other contraband is parallel to and "closely associated with" illicit arms trafficking.¹⁵² International aid officials charged with assisting women in Macedonia caught up in prostitution rings confirm that they are conducted across state and national lines; women primarily from Moldova and Ukraine are smuggled to and through Albanian rings with Macedonian and other non-Albanian cooperation.¹⁵³

In short, if borders are compromised with the assistance of the very agencies designed to control them, there is no limit to the nature of the contraband that can pass. There is a clear public interest for the Macedonian government to give high priority to investigating the allegations and denials and laying out the full record so that the country's citizens can draw informed conclusions.

I. CROSS-ETHNIC COOPERATION IN SMUGGLING

Former Interior Minister Pavle Trajanov is one of those who has directly implicated Daravelski in tobacco smuggling. He claims that Daravelski received U.S.\$10,000 to U.S.\$15,000 per truck that

crossed the border.¹⁵⁴ Trajanov also asserts that the tobacco market is shared with Albanians. DPA Vice President Menduh Thaci, he alleges, moves imported tobacco while Daravelski concentrates on counterfeits produced locally.¹⁵⁵ The cigarettes reportedly move through Kosovar, Serb and Montenegrin contacts on to the lucrative markets in Western Europe. In Kosovo, the key connection is thought to be based in Peje. Trajanov also alleges that much of the overall export market to Kosovo has been ceded to Thaci. For example, he asserts, instead of being hassled by a firm allegedly favoured by Daravelski, freight companies friendly to DPA are advantaged in Western Macedonia.¹⁵⁶

Trajanov, who holds strong views on Albanian issues, might be expected to exaggerate their take of state spoils. However, some Albanians have also been vocal with their accusations. In a formal meeting with ICG and speaking in front of the "Council of Albanian Political Parties" that he heads, Ali Ahmeti sharply criticised "our political leaders many of whom are in power to get rich".¹⁵⁷ Xhevat Ademi, a hardline Albanian opposition figure from the National Democratic Party (NDP), has publicly accused the governing Macedonian-Albanian coalition of smuggling:

Smuggling has become an international problem, and this activity is absolutely joined in by all politicians in the government. Our politicians are also involved in activities out of Macedonia. The recent wars were used by our politicians for criminal activities [including] tobacco smuggling, oil derivatives, narcotics traffic, organised prostitution.¹⁵⁸

¹⁵² "Organised crime, corruption and illicit arms trafficking in an enlarged EU", Saferworld Report, Ian Davis, Chrissie Hirst and Bernardo Mariani authors, December 2001, p. 5.

¹⁵³ Discussion with NGO officer involved in assistance to women subject to trafficking, April 2002.

¹⁵⁴ ICG interview with Pavle Trajanov, 24 July 2002. Before serving as Interior Minister, Trajanov held posts in that ministry with oversight over investigations. He now leads a political party, Democratic Alliance, that is not allied with either major Macedonian party. Trajanov is equally open with his allegations about corruption under SDSM and VMRO-DPMNE.

¹⁵⁵ Trajanov is quick to assert that tobacco trafficking also flourished under the previous SDSM government.

¹⁵⁶ As noted above, Daravelski denies that he has any connection to smuggling or to freight forwarders or that he engages in any activity designed to advantage or disadvantage firms. ICG interview with Customs Director Daravelski, 22 July 2002.

¹⁵⁷ ICG meeting with Ahmeti and Council of Albanian Political Parties, 6 March 2002.

¹⁵⁸ Ademi in *Fokus*, 19 April 2002. The NDP openly opposes the Framework Agreement because it does not

Respected media voices as well assail the DPA-VMRO-DPMNE (Albanian-Macedonian) "corrupt coalition" as inimical to common interests. Iso Rusi, the editor of the independent Albanian language weekly, *Lobi*, writes that the key achievement of DPA leaders Arben Xhaferi and Menduh Thaci was getting "Albanian participants in government their deserved share of a minimum one-third of 'governmental business'....Although totally unmasked, in their sole successful effort of filling their own pockets, the structures in power are very much at ease with each other".¹⁵⁹

One author has described the impression from "Macedonians of all stations in life [who] felt that the system is saturated with corruption. Albanian and Macedonian scholars alike castigate political parties as 'sultanistic', meaning that they are essentially political machines run by authoritarian, crooked party bosses".¹⁶⁰ If such perceptions and accusations are accurate, multinational coalition government is little more than a ploy for what *Dnevnik* calls "dividing the loot".¹⁶¹

As noted above, a senior DPA official insisted to ICG that "we do not get as much from corruption as you think".¹⁶² DPA president Arben Xhaferi consistently excuses Albanian participation in corruption as "logical when 'the Slavs' dominate the state sector. What are we to do if we don't participate in it"?¹⁶³ Rusi, the editor, has made the point that the common image of "Thaci-DPA [criminality]" is convenient for Macedonians "to

hide the real corrupt bosses of organized crime from their side".¹⁶⁴

The precise Albanian "take" of the spoils is less important than that it appears to be substantial and the result of willing participation. Xhaferi's excuse – that if we don't take the money, others will – has validity only in one sense: the fight against corruption will require a shared, cross-ethnic effort. For it to succeed, says a senior member of Ahmeti's DUI party, "we Albanians will need a determined Macedonian partner".¹⁶⁵ Macedonian politicians concerned about corruption express the same sentiments: no government can make headway against corruption unless the leading Macedonian and Albanian parties alike are committed to do so.

permit the "federalisation" (i.e. ethnic partition) of Macedonia. NDP president Kastriot Haxhirexha and Ademi have both been placed on the U.S. "watch list" of individuals Washington considers contribute to instability in the region.

¹⁵⁹ "Macedonia, one year on: Where are we going?", *Lobi*, 25 February 2002. Most such accusations do not appear to make careful distinction between whether the alleged activity relates to the acquisition of funds for political party or for personal purposes.

¹⁶⁰ "Between a Bad Peace and a Good War: Insight and Lessons from the Almost-War in Macedonia", Robert Hislope, (paper under review), p.16.

¹⁶¹ *Dnevnik* quoted cited in Hislope paper.

¹⁶² ICG interview with DPA parliamentary leader Zamir Dika, 25 June 2002. At the same meeting Dika handed over a letter addressed to ICG that denied in effect corruption accusations against the party.

¹⁶³ ICG interview with Arben Xhaferi, 23 January 2002.

¹⁶⁴ "Story for adults", Iso Rusi in *Caravan* (publication of Search for Common Ground), July 2002. Note that Rusi repeated his assertion that DPA gets one-third of government spoils in this piece.

¹⁶⁵ DUI Board Member Dr. Teuta Arifi speaking at a party press conference in Skopje, 16 July 2002.

IV. CONSPIRACY OR COLLUSION: HOW CORRUPTION HELPED BRING MACEDONIA NEAR TO WAR

The ultimate allegation about cross-ethnic corruption is that it was responsible for the conflict in 2001. Macedonian citizens, like their Balkan neighbours of all nationalities, have a fondness for conspiracy theories, and many are convinced that there was a “deal” behind the fighting. At least one senior official, President Trajkovski, has drawn a direct link between organized crime and the conflict, saying “one of the most important elements of the crisis [in 2001] was precisely organised crime in the region”.¹⁶⁶

Establishing just how corruption and crime intersect with ethnic conflict is not easy but it is critical to make the effort since policy makers are not likely to step up the fight against corruption if they are not convinced that it bears heavily on stability.

There are two general schools linking corruption to last year's conflict:

The “grand conspiracy” school. Adherents to this view believe that corrupt ruling elites schemed to create or at least manage aspects of last year's conflict in order to achieve mutual aims. Having already divided “turf” for exploitation, the most extreme theory goes, the ruling parties incited war in order to formalize the division of the country. A short-term motive is also offered: the alleged need for “controlled fighting” to distract public opinion from a burgeoning wire-tapping scandal that was threatening to bring down the government.¹⁶⁷

The “capacity building/weakening” school. Adherents of this view argue that organized crime and corrupt elements of the state combined to *build* the capacity of extremists to obtain recruits and *weaken* the

capacity and legitimacy of state institutions. The venality of the ruling parties and crime syndicates, says this school, encouraged extremists to take-up arms. Either for ideological reasons (angered that the DPA was enriching itself without advancing the Albanian agenda) or purely business reasons (powerful patrons in Kosovo perhaps angered by Thaci), they allegedly saw themselves excluded from the cosy cross-ethnic arrangement enjoyed by the ruling parties. Furthermore, the theory goes, state trafficking facilitated the access to weapons and contraband necessary to arm and finance an insurrection. A contributing element of this theory is the belief that the absence of Macedonian police from critical areas that gave insurgents the opportunity to develop bases and recruit was due to a deliberate policy of neglect – allegedly to honour DPA's request for “free space to smugglers”.

A. NO GRAND CONSPIRACY

Former Minister of Interior Trajanov is among those who appear convinced that the conflict of 2001 was an arranged affair to some considerable degree. He sketches a scenario in which the division of turf over corruption easily slides into a division of territory. In effect, he asserts, corruption functioned as a “rehearsal” for formal ethnic separation. He cites as evidence the constant pressure he says he received (while Interior Minister) from Georgievski and Xhaferi to turn a blind eye to alleged recruiting and training activities of Albanian fighters,¹⁶⁸ and what he calls the government's habit of releasing Albanian “terrorism” suspects without explanation.¹⁶⁹

¹⁶⁶ Speech by President Trajkovski at “The Balkan Club”, Skopje, 30 March 2002.

¹⁶⁷ See ICG Balkans Report number 109, *The Macedonian Question: reform or rebellion*, 5 April 2001, pp.13-14: “... in January ... [the] leader of the largest opposition party, the SDSM, accused the government of wire-tapping the telephone conversations of more than 100 public figures”. The allegations extended to the taping of diplomats, and observers agree posed a serious threat to the survival of the government – until the advent of the conflict.

¹⁶⁸ Trajanov claims that he was told to ignore a mine that was discovered to be full of weapons near Kumanovo in May 1999, that a weapons collection operation in Mala Recica (near Tetovo) was terminated by direction of the Prime Minister in July 1999, and most sensationally, that an Albanian identified by “foreign intelligence services” as an al-Qaeda operative was arrested on lesser charges because of pressure from Xhaferi and Georgievski. Trajanov insisted that the individual in question was specifically identified as an al-Qaeda operative, not simply a “terrorist”. ICG interview with Pavle Trajanov, 24 July 2002.

¹⁶⁹ These included Semi Hebibi, the suspect in the fatal attack on the Tearce village police station in January 2001, and Xhavid Hasani, released on bail in April 2000 in exchange for four Macedonian soldiers who had been kidnapped. Hasani eventually absconded and his U.S.\$100,000 bail was forfeited to the state budget after he was convicted *in absentia*.

Whether part of a grand design or not, the disengagement of Macedonian police from Albanian areas, particularly smuggling routes near the Kosovo border, was an important precondition in the buildup. One observer has said of that development:

It is public knowledge ... that the main reason why [after VMRO and DPA took office] in 1998 the government restrained from patrolling the border area after the withdrawal of UNPREDEP [the UN peacekeeping force that left in 1999] was [to permit] illegal trafficking through the border ... by DPA's Menduh Thaci in collaboration with elements very close to the leadership of VMRO-DPMNE.¹⁷⁰

The see-no-evil posture of the Macedonian police allowed smuggling villages like Tanusevci (which lies on the border, 36 kilometers north of Skopje) to become, in effect, "free territories". The village not only became the transit point for contraband, it also served as a recruiting and training base for Albanian radicals active in the nearby Presevo Valley of southern Serbia.¹⁷¹ When a Macedonian television news crew was briefly detained by uniformed Albanian guerillas, their subsequent report created a sensation, triggered the hasty dispatch of Macedonian units and sparked the first serious engagement.¹⁷²

Nevertheless, the deliberate neglect of police duties as in Tanusevci is not the same as an active conspiracy to start a war. Indeed, to establish that there was a premeditated conspiracy between VMRO-DPMNE and DPA to launch the conflict one would have to show that the NLA was part of an elaborate plan developed in common with Arben Xhaferi (and through him, with Prime Minister Georgievski). In fact, the most plausible public allegations indicate that the opposite was the case: the DPA offered bribes to persuade the NLA to *stop* fighting.

In an interview with the independent magazine *Lobi*, a prominent NLA commander known as

"Commander Hoxha" (Xhezair Shaqiri) stated that DPA Vice-President Menduh Thaci "sent his emissary, Flamur Ame, to Tanusevci to explain to us that we would have to wait for one more year [to launch the conflict], and that if we wanted he would send money to the bank or bring cash. [Thaci] sent other emissaries as well, but we refused [them.] We were not there for trade ... we had a sincere ideal and the conclusion of the war [the Ohrid Agreement] showed that nobody could corrupt us..."¹⁷³

Two external developments are sufficient to explain why Tanusevci was where fighting broke out in 2001: first, the NATO-imposed end to fighting in Presevo had closed off a theatre for Albanian rebels, some of whom were based in the village; secondly, the February 2001 accord between Belgrade and Skopje demarking the Kosovo border had enraged Albanians, giving the rebels a cause. To these, analysts have added a third, more covert reason: a possible intra-Albanian feud between Thaci and powerful groups in Kosovo, reportedly angered at his monopolisation of trade with the province at exorbitant terms. According to this reasoning, the NLA may have been given a push from patrons eager to see the DPA put in its place.

The premeditated grand conspiracy theory also does not take into account the political relationship between Xhaferi and Ahmeti. Many Albanians recall the harsh public statements made about the NLA by DPA leaders before all signed up to the "Prizren Declaration" (an accord unifying the NLA and key Albanian political leaders around a program of more rights within Macedonia rather than border changes).¹⁷⁴ And many observers believe that Ahmeti's prominent inclusion of Xhaferi and Thaci at the inaugural meeting of his "Council of Albanian Political Parties", roughly one year after the conflict began, was a way of giving his erstwhile critics

¹⁷⁰ "Crisis in Macedonia", Working Paper, Ethno Barometer 6 (Rome, 2002), p. 14.

¹⁷¹ ICG Report, *The Macedonian Question*, op. cit.: "Tanusevci became more tangled and entwined with the Liberation Army of Presevo, Medvedja and Bujanovac (UCPMB)".

¹⁷² Ibid.

¹⁷³ "Well-known NLA 'Commander Hoxha': 'Those who wanted to kill me shamed themselves'", *Lobi*, N.54, 25 February 2002. Hoxha was a member of Ahmeti's General Headquarters. The above-mentioned Hasani also hails from Tanusevci. The "sincerity" of the NLA's ideals appears to have been put to the test and found wanting at Tetovo a few weeks later; see below.

¹⁷⁴ It is worth noting that Ahmeti did not emerge as public leader of the NLA until the conflict had already broken out. The Prizren accord was brokered by American diplomat Robert Frowick, who was acting in his capacity as OSCE Special Representative; although Frowick was rapidly disowned by other international actors, the Prizren Declaration was essential to the peace process.

“amnesty” for their opposition to the NLA before they realised its popularity with their voters.

Despite the evidence to the contrary, the notion that there was a “deal” to divide Macedonia persists.¹⁷⁵ Even many of those who concede that the conflict was not the result of a grand conspiracy believe that the ruling parties colluded at least to manipulate public opinion during its course. Some note, for example, that the release of a plan to divide the country by the Macedonian Academy of Sciences and Arts (MANU) was followed “coincidentally” by the most dramatic confrontation of the conflict – the battle of Aracinovo, a village a mere dozen kilometres from Skopje. Many read Prime Minister Georgievski’s ambivalent reaction to the MANU plan as tantamount to support for partition, in the context of the heightened tensions arising from Aracinovo.¹⁷⁶

Again, closer examination provides little support for the theory. Ali Ahmeti has told ICG that the NLA occupation of Aracinovo – from where it theoretically threatened Skopje and its airport – served as a visible rejection of the MANU plan, which would have involved removal of thousands of Albanians from Skopje and Kumanovo.¹⁷⁷ A senior government adviser who was active during the period also doubts that there was collusion on any aspect of the Aracinovo drama.¹⁷⁸

The most credible example of governing party collusion involves another prominent event, the so-called offensive at the medieval fortress overlooking Tetovo on 25 March 2001. While presented to the public as a great victory, a Macedonian commander in the “Wolves” (special forces) told researchers that his forces encountered virtually no resistance.

¹⁷⁵ The notion of a VMRO – Albanian deal to divide the country dates back to the interwar period, and as well, the Fascist Bulgarian and Albanian period during World War II.

¹⁷⁶ Georgievski said of the MANU plan “I consider that their idea comes from the fact that Macedonia has been at war for three months. Actually, we have an armed rebellion by Albanians in Macedonia, and academicians have tried to find peaceful, short-term and strategic resolution of this crisis”. The prime minister added, however, that he did not accept the idea. Remarks quoted in *MILS*, 31 May 2001. See also ICG Balkans Report N°113, *Macedonia: The Last Chance for Peace*, 20 June 2001.

¹⁷⁷ ICG interview with Ali Ahmeti, March 2002. Ahmeti has made opposition to the division of Macedonia a prominent plank in the platform of his political party, the Democratic Union for Integration.

¹⁷⁸ ICG interview with senior adviser on 24 July 2002.

Young, disoriented Albanian fighters were found in trenches and hide-outs shocked that their commanders had suddenly deserted them. This Macedonian commander expressed his suspicion that there had been collusion between the ruling parties that could have placed his soldiers in danger of an ambush.¹⁷⁹

There is widespread speculation that DPA leaders, acting in concert with VMRO-DPMNE, offered a substantial sum of money to the fighters to withdraw so that the Macedonian army could claim a great “victory”. (The offensive was widely publicized as such.) A senior Macedonian official claims that as the Macedonian forces began their assault, he told the news to Xhaferi, who replied: “there is nothing to get excited about. The withdrawal has all been arranged”.¹⁸⁰

Unfortunately, the Ohrid Agreement and the subsequent progress have not ended speculation about collusion or division of Macedonia. Indeed, Ali Ahmeti has twice told ICG that he has received offers to divide the country – once well after the signing of Ohrid.¹⁸¹ More recently, collusion seems to have been in evidence during a potentially explosive confrontation on 8 July 2002, when several hundred Macedonians blocked the main highway between Tetovo and Skopje (near the village of Zelino), ostensibly to protest the unsolved fate of twelve Macedonians missing since last year’s conflict. The protest quickly incited Albanians to gather in nearby woods, some of whom reportedly fired shots. Tensions climbed immediately in nearby Tetovo, until the road barricades were removed the following day.

There are a number of indications that the roadblock was staged not as a genuine protest but to incite tension and divert attention from a critical international report on the missing persons issue.¹⁸²

¹⁷⁹ Interview with “Wolves” commander conducted by Vladimir Milcin, Director of Open Society Institute on or about 6 April 2001.

¹⁸⁰ ICG interview with former senior Macedonian official, 24 July 2002. For his part, Commander Hoxha, who is from Tanusevci, insists that rebel activity there was in response to the killing of an Albanian villager by Macedonian security forces. See Hoxha interview in *Lobi* cited below.

¹⁸¹ ICG interviews with Ali Ahmeti, December 2001 and March 2002.

¹⁸² NATO Ambassador Nicholas Biegan reportedly stated that the blockade on the Tetovo-Skopje road was obviously well organised and that the people did not gather

Members of the notorious “Lions”, a special police unit under the command of Minister of Interior and senior VMRO-DPMNE official Ljube Boskovski, were prominent in the crowd. But international sources also state that the Albanians who appeared in the vicinity of Zelino were not from that village and suggest that the two ruling parties, the Macedonian VMRO and the Albanian DPA, may have worked together to produce the incident.

In sum, while the evidence to support a grand conspiracy is thin, the likelihood is strong that the patterns of behaviour of the ruling parties – collusive (particularly on police matters) and corrupt – weakened the state and opened up opportunities for extremists.

B. CRIME, CORRUPTION AND INCREASING CAPACITY FOR CONFLICT: AN ALBANIAN OR REGIONAL PROBLEM?

The capacity building/weakening theory of Macedonia's conflict has been developed by an academic observer, Professor Robert Hislope, who argues that the symbiotic forces of Albanian organized crime and Macedonian state corruption contributed substantially to the outbreak of fighting.¹⁸³ Hislope's view is that, on the one side, endemic corruption in state structures thwarted democratic development, undermined the legitimacy of institutions, and contributed to Albanian minority frustration. On the other side, by smuggling tobacco, drugs and additional contraband, the “Albanian syndicate” supplied weapons directly or indirectly

(via its predecessor, the KLA) to the NLA insurgents.¹⁸⁴

Although Hislope acknowledges that “NLA ties to the mafia are not as obvious as [those of] the KLA”, he maintains that directly or indirectly, “the mafia was one of several sources of funding and weapons procurement”.¹⁸⁵ Additional financial needs were met from the Albanian diaspora.¹⁸⁶

Hoxha, the NLA commander, lends support to the allegations about cross-ethnic weapons acquisition, stating that “it's not true [that all our weapons came from Kosovo]; we found a great number in Macedonia and Serbia as well....The Mafia does not care about nations or religions. The Mafia only cares about money. If you have the money, you get the weapon”, he explained.¹⁸⁷

Hoxha's observation meshes with that of the small arms watchdog group Saferworld, which, in a recent study, noted that “the clear connection between organised crime and illicit arms trafficking can also be extended to conflict situations, where inevitably criminal groups are active, supplying parties with contraband military equipment and ammunition.”¹⁸⁸

Besides opening up avenues for weapons trafficking, collusion in police matters may ultimately have proved costly for the ruling parties. They reportedly engineered a change in the law concerning release of information from so-called “secret police files”. Then, just prior to the 2000 municipal elections, a senior government adviser asserts, senior VMRO officials in government released a number of files containing the names of Albanian informants

spontaneously because of the missing persons case. Biegman implied that members of the “Lions” were among the demonstrators: “It seems that there were people who recognized members of the “Lions”, although we have to confirm if they are still members”. “Biegman: It is insulting for Government that armed group sets up blockade”, *Dnevnik*, 15 July 2002. The ambassador's impressions were shared by journalists and other observers, including ICG staff at the scene.

¹⁸³ “Organised crime in a disorganised state: how corruption contributed to Macedonia's mini-war”, Robert Hislope, Assistant Professor of Political Science, Union College, Schenectady, New York. *Problems of Post-Communism*, vol. 49, no 3, May/June 2002, pp. 33-41. For an overall look at the link between corruption, organised crime and arms trafficking see, “Organised crime, corruption and illicit arms trafficking in an enlarged EU”, Ian Davis, Chrissie Hirst and Bernardo Mariani, Saferworld Report, December 2001.

¹⁸⁴ Hislope, “Organised Crime”, op. cit., pp. 1, 14. See also Tim Judah, *Kosovo: War and Revenge* (New Haven, 2000). Judah notes (p. 70) that the collapse of communism in Albania in 1991 meant that a “major new drugs route passing through Albanian-inhabited parts in Macedonia, Kosovo, Serbia-proper or, of course, Albania itself, now opened up. The significance of this in terms of the Kosovo question should not be overestimated, but still the fact that some ‘dirty money’ helped finance the Kosovar cause is more than likely, and is a fact which, for the record, should be noted”.

¹⁸⁵ Hislope, “Organised Crime”, op. cit., p. 16. He believes (p. 18) that “evidence of NLA-mafia relations is only now emerging”.

¹⁸⁶ *Ibid*, p. 15. A senior Albanian figure has told ICG of funds amounting to U.S.\$2.5 million that went missing from a collection among the U.S. diaspora.

¹⁸⁷ *Ibid*.

¹⁸⁸ Saferworld Report, “Organised crime, corruption and illicit arms trafficking” op. cit., p. 5.

affiliated with the PDP party. The DPA seized upon this information to discredit candidates from its main rival. In the views of the senior adviser, this betrayal of sources had serious security consequences after the conflict broke out as few Albanian sources dared to share information, thus leaving the government hampered by poor intelligence.¹⁸⁹

Although both elements of Hislope's "twin forces" – corrupt state structures and Albanian organised crime – are widely recognised, the relative importance of each is a frequent bone of contention between Albanians and Macedonians. Finance Minister Nikola Gruevski (a Macedonian) echoes many Macedonians when he insists: "the main generator of crime, corruption and grey economy in Southeast Europe is Kosovo, and that jeopardises not only Macedonia, but also Serbia, Montenegro, Albania and, through them, other countries in the region".¹⁹⁰

But former Finance Minister Xhevdet Hajredini (an Albanian) maintains that smuggling cannot be considered an "Albanian-only" profession: "In order to smuggle tobacco, drugs, weapons, Macedonia must be connected not only with Kosovo, but with Bulgaria, Romania, and other countries. And for that type of connection, smugglers must have official [ie. Macedonian] cooperation".¹⁹¹

In other words, while it is clear that Albanian crime partly funded the rebels' weapons, Macedonian and Albanian criminal actors, inside and outside the state, were cooperating. This alleged nexus between crime syndicates (of all nationalities) and the state is probably what President Trajkovski was referring to when he warned Balkan leaders about a state-criminal complex:

All these criminal activities [including] illegal trade in cigarettes, drugs, people, money laundering, corruption and terrorism would not have been possible without close cooperation with certain divisions and individuals, representing the governments of our countries.¹⁹²

¹⁸⁹ ICG interview with senior government security adviser, 29 July 2002.

¹⁹⁰ "Crime, grey economy, and corruption", Minister Nikola Gruevski, posting on the Finance Ministry website, 31 March 2002.

¹⁹¹ ICG interview with Xhevdet Hajredini, 16 April 2002.

¹⁹² Speech by President Trajkovski at "The Balkan Club", Skopje, 30 March 2002. Albanians also took note of

V. THE GOVERNMENT'S WEAK EFFORTS AGAINST CORRUPTION

In that same speech of 30 March 2002, President Trajkovski hinted at government complicity with criminal rings when he criticised the "confused belief that some parts of criminal structures can be our allies in achieving some minor or major social, more precisely, political goals". These remarks were widely interpreted in Skopje as criticism of the Georgievski government.¹⁹³

While Xhaferi's DPA has suffered the combined attacks of rival Albanian parties, VMRO-DPMNE been buffeted by a spate of corruption allegations in the media since the international donors conference.¹⁹⁴ The charges and counter-charges show that "corruption" has, for now at least, replaced "terrorism" as a dominant issue of Macedonian politics.

The government has responded by taking a number of steps, not all of which are encouraging. On the positive side, it set up a "hot-line" for citizens to complain about corruption. There are also proposals to implement privatisation of primary health care (as agreed in January 2002 in connection with the Law on Local Self-Government).¹⁹⁵

Three days after the Trajkovski speech, the government announced formation of a "Commission

Trajkovski's speech. Senior NDP leader Xhevat Ademi stated that "the former pawn of VMRO-DPMNE and DPA [Trajkovski], the current President, clearly pointed the finger at those involved in non-political [i.e. criminal] activities". Interview with Xhevat Ademi in "Thaci and Ljubco have made Colombia out of Tetovo", *Fokus*, 19 April 2002.

¹⁹³ The Prime Minister, who was in the audience, reportedly showed visible annoyance during the speech.

¹⁹⁴ On the occasion of the 12 March 2002 donor's conference in Brussels, ICG President Gareth Evans published an article in the *Wall Street Journal* (European edition) titled "Clean Up Macedonia". ICG also issued a media release urging donors to "Finance Peace in Macedonia, not Corruption". According to *Forum* magazine, "The title of the [ICG release] could not have been a more concise message to the international community for what has been a 'public secret' in Macedonia for years – we are sinking in corruption. ICG ... played the role of the child in the 'Emperor's New Clothes'". Cover story, "Strike against corruption!", *Forum*, 28 March 2002.

¹⁹⁵ ICG interview with Finance Minister Gruevski, 16 April 2002. See Gruevski article, "Crime, gray economy, and corruption" op. cit. for other positive developments.

for Combating Corruption". However, the questionable choice for chairman was Minister of Interior Boskovski, who has been the subject of corruption allegations himself.¹⁹⁶ As if to signal that the commission would not seriously attack domestic corruption, the government announced that its first act would be to examine the "use of humanitarian aid during the Kosovo crisis". This was a slap at Trajkovski, who played a key role in coordinating relations with the international aid community in 1999. Similarly, the government activated criminal proceedings against directors of several major enterprises, including Fersped, Pivara-Skopje, Alkaloid pharmaceuticals, Rubin-Karmin, and A-1 TV, each of which had either taken a political stance against the government or is believed to have refused to "ante up".¹⁹⁷

The government has an obligation to investigate serious allegations, including no doubt at least some of the above.¹⁹⁸ The problem is rather that the first actions of the Commission for Combating Corruption give the appearance of having transparent political motives. Fersped, for example, has links with the daily newspaper *Vest* that recently carried a story about a "palace" allegedly being built on behalf of the Prime Minister's sister-in-law.¹⁹⁹ It is unlikely that these actions will repair public confidence in institutions.

¹⁹⁶ Boskovski was publicly accused in autumn 2001 of receiving U.S.\$1 million in an illicit rice venture. He responded with an unusual denial: "I do not care about a million dollars. I earn such money on a daily basis in many ways". *Dnevnik*, 2 October 2001. Boskovski has told ICG that "if there is any evidence found about my being corrupt, I will burn myself on the city square as Jan Palach did in Czechoslovakia". ICG interview with Ljube Boskovski, 22 March 2002.

¹⁹⁷ "Criminal proceedings against directors of most powerful Macedonian companies", *Dnevnik*, 2 April 2002, and "Fersped has laundered millions of [U.S.]\$, according to Interior Ministry", *Dnevnik*, 17 April 2002. The latter article states that the Interior Ministry believes five big Macedonian companies have taken U.S.\$300 million to foreign banks. Fersped is alleged to have transferred money to its subsidiary, Fer-agent, which in turn has subsidiaries in Germany and Greece.

¹⁹⁸ Those implicating the head of A-1 television, for example, involve money laundering, and the government is not the only source for them.

¹⁹⁹ "Mayor of Skopje says the mysterious palace of PM's sister-in-law is illegal", *Vest*, 20 March 2002.

VI. HOW THE INTERNATIONAL COMMUNITY HELPS ENABLE CORRUPTION

Senior internationals in Macedonia manifest, and sometimes admit to, an almost visceral unease with the issue of corruption. In the words of one, "we dance around the problem". Another official stated, "[European] ambassadors do not want to touch this".²⁰⁰

When required to comment, international officials tend to downplay Macedonia's corruption by likening it to that in other states in transition. This encourages the government to rationalise the problem. For example, following ICG's statements at the time of the donors conference, *Macedonian Business Monthly* insisted that "'This is not only a Macedonian problem' ... was the unanimous stand in Brussels [at the conference] of Macedonian Prime Minister Ljubco Georgievski and World Bank Country Director and Regional Coordinator for Southeastern Europe Christian Poortman".²⁰¹ Finance Minister Gruevski cited a similar remark as proof that "we may not be angels, but that doesn't mean somebody else is faultless".²⁰²

In fact, as has been described above, Macedonia's performance appears to have slipped while that of neighbouring countries, including Albania, has improved.²⁰³ But comparisons to corruption indexes in other countries in transition miss the point. Few other countries are struggling to maintain the very viability of the state while using corruption as the

²⁰⁰ The World Bank is candid enough to admit its discomfiture: "While the Bank has always been concerned about the integrity of its operations, it did not explicitly talk about 'corruption' as such ... before the mid 1990s. What seems to us today an obvious issue was then considered too politically sensitive, or simply too political..." The policy continued until 1996, when President James Wolfensohn committed the Bank to fighting the "cancer of corruption". World Bank website, "Helping Countries Combat Corruption/The Evolving Role of the World Bank, World Bank Efforts".

²⁰¹ "Macedonia to declare war on corruption", *Macedonian Business Monthly*, March 2002, N°5, vol. 1, p. 4. Portman of the World Bank has repeated the line that corruption is a problem in many countries to ICG. Interview on 27 June 2002.

²⁰² Finance Minister Gruevski, "crime, grey economy and corruption", Finance Ministry web-site, posted 31 March 2002.

²⁰³ See, for example, fn. 33 above.

mainstay for “managing” interethnic relations. In a state as inherently weak as Macedonia, with a relatively small economy, mega-corruption wreaks substantially more havoc. Downplaying the special seriousness of corruption in Macedonia, therefore, is a mistake that can only encourage the government to delay reform.

An example of how the international community evades the issue is its promise to impose strict controls on donor funds. It is good that the European Agency for Reconstruction and other donor organisations are taking steps to ensure that aid goes for its express purpose. But project aid forms less than half the total commitment made by donors in Brussels in March 2002. Well over half of the quarter-billion dollar total pledged (U.S.\$165 million) was for a direct infusion into the national treasury as balance of payments assistance.

Finance Minister Gruevski, with some support from international officials, argues that the balance of payments deficit is a product of the 2001 crisis: “[By] using its foreign exchange reserves and budget surplus ... [The government] had to hastily purchase a bigger quantity of weapons, ammunition and other military equipment to defend itself from attack”.²⁰⁴ Even in the defence sector, however, corruption directly exacerbated costs and widened the deficit. In a widely reported scandal, former Defence Minister Ljuben Paunovski allegedly skimmed as much as U.S.\$6.5 million in army procurements from firms owned by his father-in-law and brother-in-law.²⁰⁵

Because money is fungible, this deficit support is and will remain a general subsidy for most government operations.²⁰⁶ In other words,

²⁰⁴ Finance Minister Gruevski writing in *Bulletin*, 12/2001, p.3. In addition to military procurement, the government had to lay out even more funds to pay for reservist call-ups in both police and the army.

²⁰⁵ See media reports of 23-25 April 2001, including “Silence before the storm in the Ministry of Defence”, *Dnevnik*, 25 April 2001. Paunovski eventually resigned and now awaits charges. He has made a number of defiant statements implying that when proceedings begin, he will reveal “what he knows” about other corrupt dealings. “Paunovski said that he would give the names, backgrounds, and role of some party officials who, according to him, are the main creators of the scandal in the Defence Ministry”, *Utrinski Vesnik*, 20 June 2001.

²⁰⁶ Negotiations with the IMF collapsed in June 2002, curtailing further deficit support by donors. However, U.S.\$50 million have already been disbursed. International

international funds, at least in part, are helping Macedonia cover sinkholes left by corrupt practices throughout government.²⁰⁷ By one estimate, as much as 40 per cent of the deficit can be directly attributable to corruption – excluding corruption’s role in reducing investment and raising costs. Another estimate puts the cost of corruption at 3 per cent of GDP.²⁰⁸

It is one kind of mistake to treat Macedonia as a “normal” transition country with respect to corruption. It is quite another to subsidise government malfeasance and not demand reform. By doing this, the international community inadvertently contributes to Macedonia’s corruption habit – signalling to those in power that “business-as-usual” will continue to be tolerated. Not surprisingly, then, many Macedonians do not see the March 2002 donors conference as an expression of international commitment to the country’s stability, but rather as a short-term expedient to obtain political cooperation.

Diplomats and organisations like OSCE do tend to believe that the delicate police re-deployment process, which depends in large part on government cooperation, will be at risk if they raise their voices too loudly on corruption.²⁰⁹ Engaging the government on corruption, however, need not always mean confrontation.²¹⁰ There is no reason,

sources say that the IMF talks collapsed for a variety of reasons including the government’s decision to go ahead with an election-year bailout of savers in the collapsed “Tat” pyramid bank and agreement to union demands for an across-the-board pay increase for state employees. They suggest that the government’s poor record on corruption was also a factor in the failure of the negotiations as it encouraged officials to look at Macedonian projections and promises with a jaundiced eye.

²⁰⁷ Interviewed by ICG, the Finance Minister acknowledged the drag that corruption has on the economy and on the national budget deficit. Interview with Finance Minister Gruevski, 16 April 2002.

²⁰⁸ “Corruption ‘eats’ 200 million dollars a year”, *Utrinski Vesnik*, 23 April 2002. *Utrinski Vesnik* cites data from a USAID-funded study.

²⁰⁹ On 8 April 2002, OSCE’s Head of Mission in Macedonia responded to ICG’s written appeal (on the anti-corruption law) and pledged continued support for the “anti-corruption strategy” to be produced by local actors.

²¹⁰ Underlying reluctance even among international financial officials to deal with corruption allegations is a fundamental misconception about “proof”. “Proof” is a legal concept. Even in courts, however, the standards of proof vary. In the U.S., “proof” ranges from the most stringent “beyond a reasonable doubt” in criminal cases to “a

for example, to believe that insisting on corruption legislation would in and of itself disrupt cooperation over new legislation. The government simply lacks the degree of domestic or international support to shirk the commitments it made at Ohrid.

In light of the condition of the judiciary, most recommended legislation does not even pose an immediate threat to corrupt practices in government. Given the media criticism it is receiving, the government might even welcome greater international engagement on corruption legislation, if only for providing it an opportunity to improve its reputation on the issue before elections.

With Macedonians still largely convinced that Ohrid is a one-way street of concessions, however, it is clear that the implementation process lacks “integrative” components – elements that can pull Macedonians and Albanians toward a common goal. The fight against corruption could be such an element, stimulating Ohrid implementation rather than hindering it. Just as ruling elites cooperate across national or ethnic lines to purloin state assets, so prominent actors in civil society – those who can help foster the cross-community bonds necessary for the Framework Agreement to work – can move across ethnic lines to mobilise citizens against corruption.²¹¹ For example, without international prompting, the “Corruption-Free Coalition” has elected ex-Minister of Finance Xhevded Hajredini (Albanian) as chairman of its coordinating board.

preponderance of the evidence” or “more likely than not” in some civil and administrative cases. Basically, standards are lowered as one moves away from criminal toward civil and administrative cases. In the present context, the standards of “proof” would appear to be even lower. The international community – World Bank, IMF, EU – are not “judges” seeking to incarcerate. They are interested parties entitled to raise questions where allegations are credible and serious. There should be some reasonable relationship between the facts alleged and the role of the international community. Given the overriding interest of the international community in developing rule of law in Macedonia, however, this standard should be easy to satisfy.

²¹¹ The potential for the anti-corruption effort to bridge the ethnic cleavage is reinforced by recent negotiations over the Law on Local Self-Government. Some Macedonian mayors, including the president of the association of mayors (and a member of the ruling VMRO-DPMNE party), broke with their government’s stance and sided with Albanians on the demand to maximise the degree of power transferred to municipalities.

In short, diplomats overstate the risks of engaging the government on corruption while understating the potential benefits of doing so.

A. TESTING INTERNATIONAL COMMITMENT: THE ANTI-CORRUPTION LAW

According to Transparency Macedonia and *Forum* magazine, the Anti-Corruption Law passed by parliament in April 2002 should form the core of the “anti-corruption strategy”.²¹² Among other things, it establishes a “State Commission for Preventing Corruption” with broad duties, including to adopt and implement a state program for fighting corruption and even to launch proceedings against corrupt officials. Unfortunately, as Transparency Macedonia points out, the law has serious flaws, including a six-month delay before the Anti-Corruption Commission is to begin its work.²¹³

Even if suitably amended, the Anti-Corruption Law would not be a cure-all, nor would the Commission immediately begin sacking corrupt officials. However, in the jargon of corruption-fighting, the law is at least an appropriate “entry point”: namely, “a place where the goals are feasible and tangible results can be realised within a time frame that builds support for further reforms”.²¹⁴ Devising and implementing the much-discussed “national anti-corruption strategy” is to be one of the Commission’s central obligations.²¹⁵ Of the avenues designed to fight corruption, passing legislation is among the simplest and least confrontational. With this small, achievable gain, an “essential lever to

²¹² *Forum* team in cooperation with Transparency Macedonia and the Sector for Research of *Forum*, “Strike against corruption!”, *Forum*, 28 March 2002.

²¹³ Transparency Macedonia had recommended ways to improve the bill while it was still before the parliament, including to ensure that the composition of the Anti-Corruption Commission would be balanced and free of political influence. See “Public Announcement – Recommendations”, Transparency International Macedonia. ICG supported Transparency Macedonia’s proposed amendments in letters sent on 3 April 2002 to the ambassadors of six major countries and two key international officials.

²¹⁴ “Anti-corruption in Transition – A Contribution to Policy Debate”, World Bank, p. 30, © 2000, posted on World Bank website.

²¹⁵ Draft law, Chapter Five – State Commission on Preventing Corruption, Article 49 (1), lines 1 and 2.

sway public and official opinion” (in the words of the World Bank) has been created.

A full-court press by the international community for an improved anti-corruption law in spring 2002, however, would have given more substance to EU External Relations Commissioner Chris Patten's pledge “to see in the former Yugoslav Republic of Macedonia, and indeed throughout the region, a really determined effort made to root out corruption. Corruption poisons political and economic life throughout the region: it has got to be tackled with total and unstinting resolve”.²¹⁶ On 17 April 2002, however – the very day that Patten (along with Javier Solana and Alain LeRoy) met with Prime Minister Georgievski and Foreign Minister Casule – parliament rejected amendments to improve the anti-corruption law.²¹⁷ The next day it unanimously passed the flawed legislation.²¹⁸

Commissioner Patten may have thrown down the gauntlet, but the international community in Macedonia has yet to pick it up. According to the European Commission Delegation in Skopje, it did not raise the law with the government, preferring instead to study the draft further. Nor does the Commission Delegation believe that it has a political platform to engage the government on corruption, preferring instead to fund projects.²¹⁹ The Council of Europe likewise preferred to await further review of the draft and the corruption situation by its GRECO arm (Group of States against Corruption) rather than lobby for amendments. EU Ambassadors discussed the law

inconclusively with the Commission Delegation.²²⁰ EU Special Envoy LeRoy, who is fully occupied with Ohrid-related laws and consequently believes others should take the lead against corruption, did raise the draft with the government, but declined to push for the changes that Transparency and the opposition proposed.²²¹

The U.S. Embassy also raised the law with officials.²²² Ambassador Butler has made several public references to the need to fight corruption, including most recently an appeal to the public to “use the next elections to seek changes if the government does not serve you”.²²³

Transparency Macedonia, the Open Society Institute²²⁴ and others have taken an initiative to develop a “Corruption-free Coalition” of key civil society actors as a means for converting mounting public disgust with corruption into productive activity. U.S. Embassy officials and other U.S.-funded officials, and OSCE, have lent their support, as has the European Commission Delegation, which has also agreed to finance Transparency's attempt to draft a national “Anti-Corruption Strategy”. The Coalition aims to mobilise support in the areas of legislation, public awareness, and public advocacy. As promising as this venture may be, it will succeed only if matched by a vigorous international effort of the sort implied by Commissioner Patten.

B. THE INTERNATIONAL LEADERSHIP VOID

Of leading embassies in Skopje, only those of the U.S. and the Netherlands report active programs to address corruption.²²⁵ USAID has a number of programs aimed at banking and accounting reform and played a key role in strengthening the Law on

²¹⁶ Speech by Chris Patten to the Western Balkans Democracy Forum, Thessaloniki, 11 April 2002.

²¹⁷ One of the amendments (along the lines of Transparency Macedonia's recommendations) would have, critically, launched the work of the Anti-Corruption Commission within 30 days. Instead, as the government wished, the Commission will not begin its work until six months after passage – well after elections.

²¹⁸ In the debate before passage of the bill, LDP leader Petar Gosev stated “I declare that the Prime Minister is corrupt and I challenge him to take me to court so that I can prove it”. Translation from television reports of parliamentary debate on 18 April 2002. Gosev has made the same or similar statements outside parliament, including to the press and in interviews with ICG, where he is not protected by immunity. See, for example, “LDP tribune in Ohrid”, *Dnevnik*, 25 February 2002, and “Petar Gosev: ‘the Bulgarophile Georgievski and his VMRO-DPMNE are already politically deceased’”, *Dnevnik*, 17 June 2002.

²¹⁹ ICG interview with EC Delegation staff, 16 April 2002.

²²⁰ ICG interview with EC Delegation official, 16 April 2002. Other officials state that EU Ambassadors are not eager to address the subject of corruption.

²²¹ ICG interview with EU Special Envoy, Alain LeRoy, 13 April 2002.

²²² ICG discussions with U.S. Embassy.

²²³ “If the government does not serve you, elections are a chance for changes”, *Utrinski Vesnik*, 27-29 April 2002. Butler emphasised that “we are working with Transparency Macedonia, the Council of Europe and the OECD to strengthen Macedonia's fight against corruption”.

²²⁴ Separately, OSI Director Vladimir Milcin has launched a multiethnic movement to fight corruption, called *Dosta E* – “Enough is enough”.

²²⁵ ICG inquiries to embassies in Skopje.

Money Laundering Prevention (and other laws affecting the financial sector). The U.S. Treasury Department has held special training on money laundering. A senior USAID official said recently that the agency is considering a program to boost "ethical awareness and moral values" as another means of combating corruption. Another official noted, however, that AID programs are designed mainly to prevent opportunities for corruption, as opposed to enhancing enforcement and punishment. The British government is funding Transparency's "National Integrity Study", a precursor to development of the "Anti-Corruption Strategy."

The European Commission Delegation will fund the drafting of that national "Anti-Corruption Strategy". The Commission's own "Country Strategy Paper" for Macedonia, however, barely mentions corruption and in contrast to Commissioner Patten's call for a "really determined effort", omits it from the list of main challenges facing the country.²²⁶ The Delegation is preparing activities on political party financing, privatisation and political influence on the judiciary but reports no specific programs as yet.²²⁷

The Netherlands finances two World Bank programs to build transparency in public administration and privatisations.²²⁸ However, despite the reported success in privatisation of Macedonia's steel works, both programs (FESAL and PSMAC), have limitations.²²⁹ FESAL (Enterprise Sector Adjustment Loan) aims primarily to "resolve" (close or privatise) the giant loss-making enterprises dating from the socialist era. In principle, this gives the Bank standing to see that resolution is transparent. In practice, the Bank is not allowed to participate in evaluating bids, so "insiders" can still get sweetheart arrangements. Furthermore, according to Bank staff, hundreds of enterprises are completely outside FESAL – and hence, any Bank scrutiny.

PSMAC is primarily a "capacity building" project, for example, to impose budget constraints on ministries.²³⁰ The Bank also maintains a regional Trade and Finance Facilitation Credit to harmonise Customs procedures. This aids mostly in upgrading information technology and physical plant, in training, and in harmonising Customs law. Bank staff concede that these efforts to improve "administrative capacity" do not address the serious problems of the Customs Service.

The Bank has a five-pronged strategy to address "state capture and administrative corruption" but actively pursues only the limited avenues mentioned and only to the extent of government interest. In the words of a Bank official, "we only work where the client wants us".²³¹

According to Transparency Macedonia Executive Director Taseva, many internationally sponsored training programs are one-time events that lack coordination and follow-up.²³² Follow-up is also conspicuously missing from two major anti-corruption initiatives: the broadly focused Stability Pact Anti-Corruption Initiative (SPAI), and the more in-depth, but limited-scope Council of Europe GRECO (Group of States against Corruption) work. The latter includes a Select Committee of Experts on the Evaluation of Anti-Money Laundering

²²⁶ At p. 3, the strategy paper says blandly that "increasing the efficiency of the state" is one of the major challenges. The word "corruption" is mentioned in passing four times. CARDS Assistance Program for Macedonia, 2002 to 2006.

²²⁷ ICG interview with EC delegation, 16 April 2002.

²²⁸ The Dutch government has a special relationship on financial matters with Macedonia, which it represents (along with other Balkan nations) in the World Bank and IMF. The Netherlands also took over command of the NATO mission on 26 June 2002, and the present NATO envoy is Dutch.

²²⁹ ICG interviews with senior World Bank staff, 19 April 2002 and prior.

²³⁰ Bank staff say the PSMAC can also be a prod to legislation. They claim that recent procurement legislation was passed because it was a PSMAC condition. Interview with Bank staff in Washington, DC, 27 June 2002.

²³¹ ICG e-mail interview with Joel Hellman, World Bank Lead Specialist, Public Sector and Governance, Europe and Central Asia Region, 15 April 2002. The five prongs of the Bank strategy are: political accountability; competitive private sector; public sector management; civil society participation; and institutional restraints. "Anti-corruption in transition – a contribution to policy debate", World Bank © 2000 p. xxii. The Bank's anti-corruption strategy addresses four key areas: preventing corruption in Bank financed projects and programs; assistance in combating corruption; mainstreaming a concern for corruption directly into country analysis and lending decisions; and contributing to international efforts to fight corruption. World Bank website, "World Bank Efforts".

²³² "The International Community and Organised Crime in South East Europe: a Southeast Europe Perspective", remarks by Transparency Macedonia Executive Director Sladjana Taseva, in London, 18 March 2002.

Measures and PACO (Program Against Corruption and Organised Crime in South-Eastern Europe).²³³

At a major regional SPAI meeting in Tirana in April 2001, the Macedonian government endorsed a range of reforms (almost 30 separate recommendations in five "pillars"). Yet, SPAI has almost no means of prodding the government to implement the recommendations except for periodic review conferences at which governments report their progress.²³⁴

The Council of Europe approach involves setting European standards; strengthening capacities through technical cooperation; and monitoring compliance with European standards. But its means for "monitoring compliance" are occasional and limited, and the concept omits completely methods for diagnosing failure to meet standards and testing (not just building) capacity.

GRECO is to prepare a report evaluating Macedonian corruption primarily in three areas: legislation, judiciary, and law enforcement. Although this is conceived as a "flexible and efficient follow-up mechanism", the government will have eighteen months to implement the recommendations after the report comes out in summer 2002, and GRECO will lack the capacity to prod it.²³⁵ For the bulk of the report's analysis,

²³³ Saferworld lists a dozen different regional initiatives dealing with the issue of organized crime and corruption. "Organised crime, corruption and illicit arms trafficking in an enlarged EU", Saferworld Report, Ian Davis, Chrissie Hirst and Bernardo Mariani, authors, December 2001, p. 31.

²³⁴ The most recent meeting took place in late April 2002 in Washington, yet Macedonia's progress in implementing the April 2001 Tirana commitments was not a particular focus at the conference. According to experts, the only other way to prod governments is where a technical assistance program is established. ICG telephone interview with SPAI staff member, 11 April 2002 and 26 July 2002. Pillars I to IV are: adoption of European and other international instruments; promotion of good governance and reliable public administration (public procurement system; public expenditure management system; financial control; civil service capabilities; public sector external audit system); criminalisation of corruption and money laundering (specialised units; investigative capacities); and promotion of transparency and integrity in business operations (preventing bribery of public officials in business transactions; promoting integrity in business). See "Anti-corruption measures in South-eastern Europe – Country Reviews and priorities for reform", pp. 25-36.

²³⁵ Instead, GRECO relies on "peer pressure" and "mutual evaluation". See "What's the GRECO?" on Council of

GRECO depends on the government's own answers to a lengthy questionnaire. The government can also review the report and make comments before it is issued.

Another regional organisation, the Southeast Europe Cooperative Initiative (SECI), was launched in 1995 to encourage close cooperation among Balkan states, especially in law enforcement. SECI claims that its centre in Bucharest is the "sole international law enforcement organisation which brings together police and customs representatives", and it lists the name of a Macedonian Customs representative.²³⁶ Yet, participation in SECI has not stemmed Macedonia's apparent slide into what is alleged to be active Customs sector racketeering. Macedonia's experience illustrates the limitations of regional programs to enhance law enforcement "cooperation" when state actors themselves are either participants in or collaborators with organised crime.

The lack of intensive follow-up to the rather limited anti-corruption efforts in Macedonia explains in part why anti-corruption programs overall have had, in the words of a thorough World Bank study, only "mixed results".²³⁷ It is fine for SPAI to set up a five-pillar anti-corruption strategy, or for the World Bank to equip its strategy with five prongs, but without greater attention to seeing to it that the recommendations within the pillars/prongs are adopted, little will be accomplished. For the moment, no international agency or actor in Macedonia seems to believe that leading or even coordinating the fight against corruption is its responsibility.

Anti-corruption efforts also suffer from too much strategy and not enough tactics. A senior World Bank official speaking at a major conference on corruption, candidly noted that "25 out of 28 countries regionally have 'anti-corruption

Europe, GRECO website. Evaluators also conduct one, brief on-site set of interviews and review data provided by other sources. However, staff say that the answers to the questionnaire form the core of the report. Another Council of Europe organisation, the Select Committee on the Evaluation of Anti-Money Laundering Measures, also conducted an evaluation and issued a report in June 2000.

²³⁶ See SECI web-site, www.secicenter.org, "Mission, Vision, Objectives of the SECI Center". SECI also enables prosecutors in the region to cooperate.

²³⁷ "Anti-corruption in transition – a contribution to policy debate", World Bank © 2000, p 15.

strategies', yet results are paltry".²³⁸ Such strategies are sometimes feel-good exercises for donors who can put a "tick-in-the-box" that "something is being done".²³⁹ Most stress legislation and the build-up of "capacity". Yet in Bosnia & Herzegovina, seven years of seminars, training sessions, and "capacity building" have not yielded a single major corruption or organised crime conviction – even where the international community has supplied the evidence.²⁴⁰

Professor Marjanovic says, with understandable acerbity:

[for] God's sake, we have been [harmonising with the EU] all possible laws in the country. The Criminal Law was supervised by the Council of Europe and it was found flawless – in divine harmony with European criminal legislation! And what has happened? Nothing! The problem is that no one gives a damn about [the law] in practice.²⁴¹

Even within the laws themselves, there are loopholes. Transparency Macedonia's Taseva believes, for example, that not nearly enough attention is paid to honing rules so that government can take the profit out of corruption by confiscating ill-gotten gains.

Transparency Macedonia argues that, overall, "the role of the international community in supporting and monitoring anti-corruption activities is insufficient".²⁴² Fortunately, however, some senior U.S. officials appear to have grasped the link between erosion of rule of law in Macedonia and the country's stability:

Today, the greatest threat to stability comes not from states but from their inadequacies – the inability of the new democracies to control borders, to promote rule of law, and to respond to the needs and insecurities of their citizens. One year ago, these same inadequacies were exploited by violent extremists who nearly succeeded in causing another Balkan war, this time in Macedonia.²⁴³

Yet, these lucid warnings are not matched by action. Unless the international community matches its determination to obtain full implementation of the Framework Agreement with serious efforts to tackle corruption, that document so painfully developed at Ohrid risks becoming a paper peace, awaiting the next conflict to be torn up and rewritten. By dodging corruption, the international community risks repeating its fundamental mistake in Macedonia over the past decade: namely, interpreting the absence of open hostility as "progress", and sweeping difficult problems under the rug.

²³⁸ Senior World Bank official speaking at the OECD-sponsored conference of the Anti-Corruption Network, Istanbul, 31 March 2002.

²³⁹ Ibid. It must be noted again that Macedonia has already made a range of legislative and administrative commitments at the SPAI meeting in Tirana in April 2001.

²⁴⁰ ICG discussion with OHR official from "Anti-Fraud Unit", 29 March 2002.

²⁴¹ Djordji Marjanovic in *Dnevnik*, 22 April 2002. Echoing Marjanovic's view were these words from a participant of the Republic of Georgia at a recent anti-corruption conference: "We already have plenty of laws. The problem is that we don't enforce them". OECD-sponsored conference of the Anti-Corruption Network, Istanbul, 30 March 2002.

²⁴² "Anti-corruption in the Republic of Macedonia", paper by Transparency Macedonia, December 2001, p.2.

²⁴³ "U.S. Strategy for the Balkans", presentation by Greg Schulte, National Security Council Senior Director for Southeast Europe, Georgetown University, Washington, D.C., 20 March 2002.

VII. CONCLUSION: FINDING WAYS TO FIGHT CORRUPTION NOW

This report has charted:

- how Macedonian stability suffers from endemic, bi-ethnic corruption in government; and
- how the international community, in the belief that there is a contradiction between confronting the government on corruption and gaining its cooperation on the Ohrid agenda, does not wish to deal with the problem except with the “usual” programs.

ICG believes that this latter approach is mistaken. Far from being in conflict with Ohrid, replacing a corrupt spoils system as the basis for managing inter-ethnic relations should be a vital priority.

However, devising just where and how the international community should apply its efforts is not nearly so evident. As discussed, the trend in corruption-fighting stresses a “holistic, multidimensional approach” (e.g. five prongs for the World Bank, even eleven pillars for Transparency International). A common theme has been “capacity building” – strengthening the legal framework and institutional capabilities, as opposed to prosecuting and convicting corrupt individuals. Another truism has been that “fighting corruption is a long-term process without quick fixes”.

Such comprehensiveness and long time scales may be appropriate for many transition countries, but not one that is trying to work its way through inter-ethnic conflict in which corruption features so insidiously. The “long-term” and “holistic” approaches contain an inherent flaw: by their protracted nature, they diminish any sense of urgency. If Macedonia must advance on eleven separate fronts to make progress (as Transparency International's full program would suggest), then no one will expect results soon. The question is whether Macedonia has that much time to wait. If the international community adheres to the current anti-corruption orthodoxy, the government will always have a ready excuse with which to defend lack of progress. Transparency International (headquarters) seems to concede this point by highlighting the

importance of getting some “quick wins” to bolster public support and confidence.²⁴⁴

Other paralysing concepts are the frequent insistence on “ownership” (by local citizens) and “partnership” (with the local authorities.) While local consultation is important, the term “ownership” is increasingly employed by internationals as an excuse to remain idle. In Macedonia, which has a plethora of local NGOs and yet a weak civil society, international rhetoric about “ownership” tends to become self-serving. Without internationals leading the charge (or at least actively engaged throughout), civil society efforts like the “anti-corruption coalition” will go nowhere. Indeed, one glaring problem is the absence of any international organisation or state which will stand up and take a leadership role even to coordinate efforts.

A similar caution applies to the demand for “partnership” with the authorities. Where, as in Macedonia, it is clear that the government has no interest in joining the fight, it is naïve to insist on “leadership from the top” and “civil society-government partnership”.²⁴⁵ The leadership is very much part of the problem in Macedonia, not the solution.

The Macedonia chapter of Transparency International (TI) is presently preparing a study on the country's “National Integrity System,” to be followed by a “National Anti-Corruption Strategy” with input from many sources. This methodical project will uncover areas deserving of emphasis. Experience from other countries, however, suggests that even the most elaborate and comprehensive strategy is no substitute for identifying priority action steps that the international community and civil society can take *now*. A good deal of the TI strategy will likely focus on improving Macedonia's laws, for example recommending changes in evidentiary rules and elimination of the present requirement that, for conviction, a corrupt official must virtually be caught in the act. Passage of laws against “illicit enrichment” and enabling

²⁴⁴ “TI Source Book 2000”, Chapter 29: Lessons Learned – A Progress Report; Item 3 and *passim*.
www.transparency.org/sourcebook/index.html

²⁴⁵ The Bank stresses that “a serious anticorruption program cannot be imposed from the outside, but requires committed leadership from ... the highest levels of the state.... [A]ny effective program must be supported from the top”. “Anti-corruption in transition – a contribution to the policy debate”, p. xxx, World Bank © 2000.

confiscation of ill-gotten gains are other important recommendations that may emerge from this study.

Nevertheless, there are two problems with emphasis on legislation. First, as noted above, there are few serious follow-up mechanisms for the raft of laws already proposed by SPAI, GRECO and others.¹ Such reviews as there are tend to focus more on whether a specific law is passed than on the quality of its provisions or, most importantly, its implementation. At best, there is reliance on little more than "peer pressure" to encourage genuine compliance.

Secondly, while some new legislation is badly needed, Macedonia does not lack the legal framework to prosecute cases now. Political influence over the prosecution and courts and within the police appears to be a significant reason why so few cases are pursued. In an interview with ICG, the Public Prosecutor, Stavre Djikov, offered no convincing reason why some of the most egregious instances of corruption are not prosecuted.²⁴⁶ An effective strategy needs to focus on activating the legal system, not just handing it more laws. As TI (headquarters) observes, "[many] legislatures have passed new ... laws [to fight corruption] with great fanfare... But laws are failing in every country where corruption is systemic, and they fail more from lack of law enforcement than from any inadequacies in the laws themselves".²⁴⁷ TI adds, "there is an inherent contradiction in trying to use a corrupt judicial system to uphold the Rule of Law".²⁴⁸

ICG's recommendations (below) are designed to complement the emerging national strategy with actions that not only build capacity, but also test it. Most of these steps can be taken quickly if there is international will and require only modest expenditures.

It is one thing to devise sensible solutions, another to get agreement on them. The coming election campaign presents an opportunity for swift progress. The fact that the government is on the defensive gives the international community rare leverage to raise these matters with it. Diplomats can keep the discussions discreet, going public (as the IMF did) only if there is failure to close a deal. Government leaders can hardly afford to give the opposition the gift of appearing obstinate about reasonable proposals to build transparency and accountability.

An additional advantage of acting now is that pre-election commitments can be structured to bind any incoming government. Opposition parties should be asked to give their imprimatur to the same reform commitments as the government and even to sign on to the National Anti-Corruption Strategy (when it emerges). On the other hand, the international community is likely to get less cooperation if it waits until after the elections to address the issue with whatever party or parties has acquired a mandate.

Urge the Macedonian government to accept appointment of "international watchdogs" to work inside institutions that are particularly sensitive for corrupt activities, including the Customs Directorate, the Health Fund, and the Ministry of Economy.

If Macedonia is to stabilise, it must have democratic, accountable control of its borders. Returning police and army to former crisis areas and to the borders (as stipulated under Ohrid) makes little difference if all too many of their personnel acquiesce or even participate in trafficking. Likewise, insisting that the Finance Ministry improve revenue collection or decentralising the health care system make little sense if government funds are siphoned off to political parties and individuals.

The political parties have already accepted the watchdog concept in the side agreement reached on the Health Fund in conjunction with passage of the Law on Local Self-Government. The World Bank rejects the watchdog concept and is unwilling to fund it because it fears the individual will prove to be ineffective and the existence of the position may be used, in effect, to produce a false sense of security with regard to corruption. These are legitimate concerns, but the innovation is worth a try, and the Bank should reconsider. The international community should be prepared to pick up the costs for similar watchdogs in other government

²⁴⁶ Interview with Public Prosecutor Stavre Djikov, 25 April 2002. Djikov cited the on-going prosecution of Minister of Defense Paunovski as an example of an effort to pursue a sensitive case. That adequate legal grounds were found to prosecute Paunovski does indicate that prosecutions are possible. That more cases have not been pursued, however, suggests that Paunovski may have fallen out of favour with the political establishment and that political criteria determine which prosecutions are or are not pursued.

²⁴⁷ "TI Source Book 2002", Chapter 29: Lessons Learned – A Progress Report, Item 26., TI web-site www.transparency.org/sourcebook/index.html.

²⁴⁸ Ibid., Item 27.

institutions where corruption questions or temptations are considerable. The responsibilities of those watchdogs can be structured along the lines of the Health Fund model. The key elements are that the watchdogs should be physically located within the government offices, in close proximity to the most senior officials, and have full access to information and data.

These international experts will not instantly wipe out corruption, but they will be able to assess actual procedures and performance against laws and regulations. If they are ignored, they can ask why. They can guard against political interference much as has happened in Macedonia's Central Bank, where, staffers say, the presence of the IMF Resident Representative provides on-site expertise and helps fend off political interference.²⁴⁹ The viability of inside watchdogs can be demonstrated by the success of USAID-sponsored auditors who are housed inside Croatia's Privatization Department. Auditors offer a "secondary review" of privatisation bids, providing a check on "insider deal-making".²⁵⁰

Such "watchdogs" strike a balance between over-reliance on local officials to withstand pressure and inducements and international over-involvement. Responsibility remains with the government; while the watchdog serves as confidante, adviser, and vital conduit to the international community, not a shadow administrator. The concept avoids both the "ownership" fallacy (asking Macedonians to do more than they can) and the "creeping protectorate". Relative to the costs of permitting malfeasance, and the perception of malfeasance, to continue, watchdogs are also a potential bargain.

Urge the Macedonian government also to accept appointment of "international watchdogs" inside institutions that are particularly sensitive for the punishment and deterrence of corruption, including the Public Prosecutor's Office and the Judiciary.

There will be no overall progress on fighting corruption unless egregious cases are prosecuted. In parallel with the effort to streamline and improve the legal code, Macedonia needs to improve the performance of its prosecution, police and judiciary. Building "capacity" (training new police cadets, for example, and eventually improving the intelligence capacity of the police to gather better and more timely information that can be used in fighting corruption as well as other serious criminal activity) is essential for the medium-term but will not address neglect and political tampering that exists now.

Inserting watchdogs into these key areas would help to uphold standards and minimise political interference. The Public Prosecutor has told ICG he would welcome the appointment of such an individual to his office.²⁵¹ Experience from the Office of the High Representative in Bosnia Anti-Fraud unit suggests the efficacy of having internationals *within* the judicial system to encourage it to withstand political interference and overcome systemic lethargy. At the same time, watchdogs within the justice system could also assist in avoiding vindictive prosecutions of political enemies of the government of the day.²⁵²

Appoint an EU Anti-Corruption Adviser (ACA).

Just as EU Special Envoy LeRoy's day is filled trying to get the government and parliament to draft and pass meaningful Ohrid legislation, so the Adviser would work to realise the anti-corruption

²⁴⁹ Governors can escape demands for favours by saying, "I'll never get this one by the IMF guy". Another precedent exists in the Defence Ministry where a British Brigadier serves as an in-house adviser. The Defence Ministry has a far better reputation for reliability and cooperation than its counterpart, the Ministry of Interior. Another success story is in Croatia, where a Price Waterhouse team of experts sits inside the Privatisation Fund, helping to ensure the fullest transparency and optimal disposal of state-owned assets. Interview with Price Waterhouse in Zagreb, 14 June 2002. Telephone conversation with USAID Croatia, which funds the project, 28 June 2002.

²⁵⁰ Interview with KPMG officers in Zagreb, Croatia 14 June 2002. Follow-up conversation with USAID officials confirmed the viability of KPMG's secondary review of bids. Telephone interview USAID official in Zagreb, 28 June 2002.

²⁵¹ Interview with Public Prosecutor Stavre Djikov, 25 April 2002.

²⁵² Analysts say that this was the problem with a corruption crackdown in neighbouring Bulgaria following the last elections: "As elsewhere in Southeastern Europe and the former Soviet Union, the Bulgarian government's proclaimed crackdown on corruption sometimes appears to be more a means of undermining the reputation of its predecessor than a dispassionate attempt to eradicate an evil that sabotages economic progress, especially when those implicated belong to, or have close ties to, the ruling regime. For that reason, the public at large tends to regard any proclaimed crackdown on corruption with either cynicism or indifference". "Bulgaria and Corruption", Ulrich Buechenschuetz, Radio Free Europe, 28 June 2002.

agenda.²⁵³ The ACA would lobby ministers and parliamentarians to draft loophole-free laws and act as the lead political conduit for the “international watchdogs” when they encounter obstacles. Likewise, the ACA would alert key embassies, the European Commission Delegation and high international officials if facing serious obstacles in his or her own work. To provide significant leverage for dealing with Macedonian officials, the ACA should be authorised to recommend suspension of donor funding as appropriate, and major donors should pledge to respect such recommendations. The ACA would also usefully coordinate with, assist and support the anti-corruption efforts of civil society groups and the initiatives of international bodies such as the Stability Pact and the Council of Europe.

Several leaders of Macedonian civil society have publicly endorsed the ACA idea, including Transparency Macedonia Executive Director Sladjana Taseva, Professor Vlado Kambovski and Professor Djordji Marjanovic.²⁵⁴ In a meeting with ICG on 6 March 2002, Prime Minister Georgievski gave his immediate assent to the concept although subsequent statements have indicated less enthusiasm for pro-active measures.²⁵⁵

Condition financial aid to the government, in particular all balance of payments and budget support, on its seriousness in undertaking anti-corruption reform.

The March 2002 donors conference not only produced pledges for reconstruction and Ohrid implementation but also for Macedonia's balance of payments deficit. In fact, the largest single component of promised aid was a cash infusion for this purpose. Even though donors have held back further payments since the collapse of the IMF negotiations, U.S.\$50 million had already been

dispatched. Aid or credits not yet disbursed (other than what is directly connected to putting people back into their homes or implementing Ohrid), should specifically include commitments and conditions with respect to corruption – for example, acceptance of the international watchdogs and the Anti-Corruption Adviser discussed above.

It will be necessary, though admittedly difficult, to develop in cooperation with the Macedonian government realistic benchmarks to assess both the good faith and the effectiveness with which it attacks corruption. It will likewise be a complex matter for donors to make calls on questions such as what percentage of possible aid might be freed up by what degree of less than full zeal or unambiguous success in government efforts. However, there is simply no reason for donors and international financial institutions to be bashful about direct discussion with a government that seeks major financial assistance. Merely to look askance at corruption while giving soft aid would truly be to act as one of the enablers of a corruption habit that weakens both the economy and the security of the country.

Support the Anti-Corruption Commission

The anti-corruption law passed in April 2002 provides for creation, though only after six months, of an Anti-Corruption Commission. By the end of 2002, parliament is obliged to pass the Ohrid-prescribed “Law on the Public Attorney” to reinforce the powers of the already extant Ombudsman.

Temptation to devolve the anti-corruption fight on the Ombudsman should be resisted. That official already has a very large responsibility for protecting Ohrid-enshrined rights (for example, safe-guarding the principle of equitable representation) that will inevitably require the majority of the office's time. By contrast, the Commission is intended to focus exclusively on anti-corruption efforts. It should be regarded as the primary government institution for that purpose and accordingly worthy of financial and other support. No specific international funding for the Commission is currently envisaged, however. This should be corrected so that it can begin to operate effectively as soon as it is launched in October 2002. Donors also should exercise vigilance and apply pressure as necessary to ensure that those appointed to the Commission are qualified and not simply “political plants”.

²⁵³ The European Union, because of the extent of its interests and programs in Macedonia, could most usefully establish and operationalise the ACA function and therefore take a leading role in the effort to achieve good governance. Whether the holder of the position should ultimately report to the Council or the Commission is a matter best left to internal EU decision making.

²⁵⁴ “ICG demands foreign assistance for corruption”, *Utrinski Vesnik*, 13 March 2002. Marjanovic quoted in *Aktuel* interview, op. cit.

²⁵⁵ The idea was presented to the Prime Minister in terms of an adviser who “would function just like [EU Special Envoy] LeRoy, but in the area of corruption”.

Establish result-oriented goals on convictions and confiscations.

Anti-corruption efforts in Macedonia need to focus not only on legislation and capacity building, but also on convicting wrongdoers and confiscating illegally obtained property. Instead of being lulled into complacency each time parliament passes a new law, the international community (and civil society) should set targets relevant to those laws that will keep pressure on government institutions, including the courts, to act on them.

Support Transparency International Macedonia's efforts to develop an anti-corruption strategy and the related effort to build an "anti-corruption coalition".

Transparency International has thus far identified four "immediate" legislative measures:

- amending the Anti-Corruption Law to enable the National Anti-Corruption Commission to get off to a fast start;
- amending Article 17 of the Constitution to permit wire-tapping;
- introducing confiscation measures into the criminal code; and
- improving evidentiary provisions in the criminal code

It has also identified three medium-term legislative measures:

- drafting and passing a law on conflict of interest;
- drafting and passing a law on free access to information; and
- establishing regional cooperation on anti-corruption initiatives.²⁵⁶

TI further urges restrictions on the "discretion" of public officials, such as a "first-come, first-served" policy to correct abuses in the sale of contingents.

Thus far only the European Commission Delegation, and the U.S., Dutch and British

Embassies have shown much interest in or financial support for TI Macedonia's efforts. If the fledgling civil society initiatives are to succeed, a wider international response is essential. In particular, once the strategy is drawn up and priority legislation and other measures are identified, civil society will need strong international backing to convert them into public policy and law.

Engage Albanian parties and civil society in the anti-corruption effort.

Because most efforts to deal with legislation and government reform are Skopje-based, by definition there is a tendency to concentrate on the Macedonian community. Albanian legislators and certain experts like Xhevat Hajredini, the former defence minister and present chairman of the "anti-corruption coalition", may be involved in the campaign, but not the wider Albanian community. Polls show, however, that Albanians are increasingly aware of corruption and as disgusted by it as their Macedonian counterparts.

Whereas Ohrid implementation tends to be viewed by many in the country as a zero sum game to meet Albanian demands, engaging with Albanian political parties, civil society and the media on the corruption issue provides an opportunity for dialogue and cooperation between the two main ethnic groups. This can help Macedonians begin to see Ohrid not simply as a device for "terrorists to pose as human rights fighters", but as a means for creating more accountable institutions at all levels of government.

Relax IMF restrictions on hiring additional personnel in the State Auditor's Office.

Officials in the State Auditors Office argue plausibly that budgetary restrictions severely crimp their ability to conduct even a small portion of the audits they are legally obliged to perform. Even so, it appears they have been able to uncover serious improprieties. As a vital component for establishing the basis for further investigation into and prosecution of corruption cases, the State Auditor's Office should be exempted from the strict government-wide hiring restrictions imposed on IMF demand. A more effective State Auditor's Office can become a "budget multiplier" by producing revenue savings that more than offset the cost of additional staff.

²⁵⁶ "Action Plan – Coalition: Corruption Free Macedonia", 22 April 2002, p.2. While identified by the European Commission Delegation rather than TI, a law on political party financing would also seem a worthwhile target.

“Twinning” of international auditing experts should also be considered for this office.

Incorporate specific “follow-up” elements in all anti-corruption training programs.

Lack of follow-up is a common problem with the programs that several states and international organisations run to train local officials in techniques to reduce corruption. The course is given, the instructor leaves, and no one checks to see how or if the new methods are applied. If it is to be effective, anti-corruption training must incorporate some form of follow-up. To escape some of the costs of bringing trainers back to Macedonia, donors could partner with TI or other NGOs to monitor implementation.

Limit the scope of incumbent political parties to make appointments.

Restricting the opportunities for political patronage has to be a priority in any struggle for good governance. While the benefits from training and development of a professional administration may take years to realise, there is no reason why a legislative constraint cannot be established now to prevent the top-to-bottom cadre changes common in Macedonia when a new government takes power. The establishment of minimum competence criteria for such appointments as remain within political gift would also help to reduce debilitating instances of nepotism.

Establish incentives for fighting corruption.

Punitive enforcement provisions should be complemented by incentives for good governance. These can include higher salaries,²⁵⁷ deferred compensation (e.g. larger pensions for those who retire without having infringed the rules), and “whistleblower bonuses”.²⁵⁸ Additionally, the international community might consider funding special awards for:

- ❑ journalists who report effectively on corruption;
- ❑ politicians, judges and administrators who have exemplary records on corruption issues; and
- ❑ members of civil society who effectively mobilise public opinion against corruption.

Skopje/Brussels, 14 August 2002

²⁵⁷ While improving the compensation of officials in positions especially subject to corruption temptations is reasonable on its face, Macedonia's budget situation is such that it is unlikely the IMF would approve significant government salary increases.

²⁵⁸ See various writings on this subject by analyst (and former adviser to Macedonian Minister of Finance Nikola Gruevski) Sam Vaknin, e.g. “Greek investments in the Balkans”, UPI, December 2001. Available at <http://www.balkanlands.com>.

APPENDIX A

MAP OF MACEDONIA



APPENDIX B

ABOUT THE INTERNATIONAL CRISIS GROUP

The International Crisis Group (ICG) is a private, multinational organisation committed to strengthening the capacity of the international community to anticipate, understand and act to prevent and contain conflict.

ICG's approach is grounded in field research. Teams of political analysts are located within or close by countries at risk of outbreak, escalation or recurrence of violent conflict. Based on information and assessments from the field, ICG produces regular analytical reports containing practical recommendations targeted at key international decision-takers.

ICG's reports and briefing papers are distributed widely by email and printed copy to officials in foreign ministries and international organisations and made generally available at the same time via the organisation's Internet site, www.crisisweb.org. ICG works closely with governments and those who influence them, including the media, to highlight its crisis analyses and to generate support for its policy prescriptions.

The ICG Board – which includes prominent figures from the fields of politics, diplomacy, business and the media – is directly involved in helping to bring ICG reports and recommendations to the attention of senior policy-makers around the world. ICG is chaired by former Finnish President Martti Ahtisaari; and its President and Chief Executive since January 2000 has been former Australian Foreign Minister Gareth Evans.

ICG's international headquarters are at Brussels, with advocacy offices in Washington DC, New York and Paris and a media liaison office in

London. The organisation currently operates eleven field offices with analysts working in nearly 30 crisis-affected countries and territories and across four continents.

In *Africa*, those locations include Burundi, Rwanda, the Democratic Republic of Congo, Sierra Leone-Liberia-Guinea, Somalia, Sudan and Zimbabwe; in *Asia*, Indonesia, Myanmar, Kyrgyzstan, Tajikistan, Uzbekistan, Pakistan and Afghanistan; in *Europe*, Albania, Bosnia, Kosovo, Macedonia, Montenegro and Serbia; in the *Middle East*, Algeria and the whole region from Egypt to Iran; and in *Latin America*, Colombia.

ICG raises funds from governments, charitable foundations, companies and individual donors. The following governments currently provide funding: Australia, Canada, Denmark, Finland, France, Germany, Ireland, Luxembourg, the Netherlands, Norway, the Republic of China (Taiwan), Sweden, Switzerland and the United Kingdom.

Foundation and private sector donors include The Ansary Foundation, The Atlantic Philanthropies, Bill and Melinda Gates Foundation, Carnegie Corporation of New York, Charles Stewart Mott Foundation, Ford Foundation, John D. and Catherine T. MacArthur Foundation, John Merck Fund, Open Society Institute, Ploughshares Fund, Ruben and Elisabeth Rausing Trust, Sasakawa Peace Foundation, and William and Flora Hewlett Foundation.

August 2002

APPENDIX C

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* The Algeria project was transferred from the Africa Program in January 2002.

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