

## NATIONAL PROGRESS REPORT 1998

<b>A. INTRODUCTION</b>	<b>2</b>
A) PREFACE	2
<i>The Context of the Progress Report</i>	2
B) RELATIONS BETWEEN THE EUROPEAN UNION AND LATVIA	3
<i>Recent Developments in Bilateral Relations</i>	3
<i>The Enhanced Pre-Accession Strategy</i>	3
<b>B. CRITERIA FOR MEMBERSHIP</b>	<b>4</b>
1. POLITICAL CRITERIA	4
1.1. <i>Democracy and the Rule of Law</i>	4
The Parliament ( <i>Saeima</i> )	4
The Executive	4
The Judicial System	5
1.2. <i>Human Rights and the Protection of Minorities</i>	5
Civil and Political Rights	6
Economic, Social and Cultural Rights	6
Minority Rights and the Protection of Minorities	7
2. ECONOMIC CRITERIA	7
2.1. <i>The Economy in the Perspective Member State</i>	7
Recent Macroeconomic Indicators and Structural Adjustments	7
The Existence of a Functioning Market Economy	10
The Capacity to Cope with Competitive Pressure and Market Forces	11
3. ABILITY TO ASSUME THE OBLIGATIONS OF MEMBERSHIP	12
3.1 <i>Internal Market Without Frontiers</i>	12
The Four Freedoms	12
General Framework	12
Free Movement of Goods	13
Free Movement of Capital	14
Free Movement of Services	14
Free Movement of Persons	16
Competition	16
3.2 <i>Innovation</i>	17
Information Society	17
Education, Training and Youth	18
Research and Technological Development (RTD)	18
Telecommunications	18
3.3 <i>Economic and Fiscal Affairs</i>	19
Economic and Monetary Union	19
Taxation	19
Statistics	20
3.4 <i>Sectoral Policies</i>	21
Industry	21
Agriculture	21
Fisheries	23
Energy	23
Transport	24
Small and Medium Enterprises	25
3.5 <i>Economic and Social Cohesion</i>	25
Employment and Social Affairs	25
Regional Policy and Cohesion	26
3.6 <i>Quality of Life and Environment</i>	27
Environment	27
<b>D. SUMMARY AND CONCLUSION</b>	<b>35</b>
<b>Annex 1. APs/NPAAs: GLOBAL ASSESSMENT AND IMPLEMENTATION</b>	
<b>Annex 2. STATISTICAL DATA</b>	
<b>Annex 3. AGRICULTURE</b>	

## A. INTRODUCTION

Since the publication of the Commission's *Avis*, Latvia has shown impressive progress.

The legal framework for approximation of the *acquis* is developing steadily and implementation of legislation has contributed to administrative capacity building efforts.

Latvia's macroeconomic indicators are favourable. GDP growth is one of the highest among the candidate countries. In 1997, GDP growth was 6.5%. The current level of GDP growth shows every sign of being sustainable in the coming years.

The Government's commitment to fiscal discipline is reflected in the balanced budgets set for 1998 and 1999. The 8.4% inflation level in Latvia is the one of the lowest among the applicant countries. 12-month inflation in May 1998 reached 5.4%.

Standard & Poor's "BBB" rating for long-term foreign currency debt is an expression supporting international investor confidence and the increasing level of foreign direct investment follows suit.

The privatisation process is almost completed. 95% of Latvian state companies are being privatised. Over two thirds of Latvian GDP is already generated by the private sector. Following demonopolisation linked to privatisation and development of market-oriented business structures, small-and-medium sized enterprises (SME's) are responsible for about one half of Latvia's GDP while employing roughly two thirds of Latvia's residents.

Liberalisation of the land market was completed in May 1997. In 1998, the share of investments in real estate reached 23.3% of GDP. The total amount of foreign direct investment inflow in 1997 constituted approximately USD 340 per capita, thus Latvia is one of the leading Associated countries in this respect.

Latvia is expected to become a full fledged member of WTO by the end of 1998. Latvia aligns itself with the EU policies within the WTO.

The democratic political system established in Latvia after August 1991 has provided a stable foundation for the process of reforms. Several changes in Government have taken place, but the Government has retained its firm commitment to the strategic target of EU accession. The Government works closely with the Parliament (Saeima) on EU integration issues. The tradition of pro-EU policies will remain firmly in place after the national elections on 3 October 1998.

Taking into account Latvia's multiethnic society, one of the main policy aims of the Government is to create a unified and integrated society. A National Program for Integration of Society is under preparation and is scheduled for presentation by October 1998. The state supports 20 minority cultural societies and secondary education in 8 minority languages. In order to accelerate the naturalisation process, in June 1998, the Saeima adopted amendments to the law *On Citizenship*. The amendments provide for elimination of the so-called "windows" system and granting of citizenship to state-less children born after 21 August 1991. Other simplifications to the naturalisation procedure had already been made earlier. One of the crucial elements in the integration of minorities is Latvian language training. Supported by a UNDP and PHARE programmes, the National Program for Latvian Language Training has already reached more than 40,000 persons.

### a) Preface

#### The Context of the Progress Report

The Government is committed to ensure steady economic growth, sustainable political and social development and national security. Full membership of the European Union is the target of the reform process of Latvia and the Government's intention is to be ready to assume fully the obligations of membership of the EU.

The Progress Report will show that Latvia's reaction to the Commission's *Avis* is consistent, constructive and methodical and that since the *Avis* major progress has been achieved in meeting the Copenhagen criteria. Analysis and planning of the integration process is found in the Government Action Plan, the EU Integration Strategy, as well as the Third National Program for the Integration into the EU (National Program for Adoption of the *Acquis*). Latvia is one of three applicant countries which have elaborated a comprehensive Medium Term Economic Strategy and a Strategy in Third pillar issues. A National Program for Integration of Society, based on results of comprehensive research completed this spring, will be released this autumn.

A horizontal structure for co-ordination of the EU integration process has been developed. Effective management is ensured by the European Integration Council, the Council of Senior Officials, European Integration Bureau and the Ministry of Foreign Affairs. Structures responsible for EU policy implementation and co-ordination operate in each line ministry.

The National Progress Report describes Latvia's integration into the EU, based on the priorities outlined by the Commission. The structure of the Progress Report reflects that of the Commission's *Avis* and covers the period from the beginning of 1997. It includes the developments planned for the remaining months of 1998.

## **b) Relations Between the European Union and Latvia**

### **Recent Developments in Bilateral Relations**

With the entry into force of the Europe Agreement in February 1998, bilateral relations between EU and Latvia have entered a new phase. The Europe Agreement provides a framework for political, social, economic dialogue and steady integration of Latvia into the EU.

The EU-Latvia Association Council held its first meeting in February 1998. During the EU-Latvia Association Committee meeting held in May 1998, the EU side appreciated the meaningful developments in Latvia with regard to the short term priorities stated in the Accession Partnership - specially mentioned were the liberalisation of naturalisation procedures, the speed of the privatisation process, harmonisation of legislation, and the National Programme for Adoption of the *acquis*. During its second meeting in June 1998, the EU-Latvia Joint Parliamentary Committee held discussions on the implementation of the Europe Agreement and Latvia's preparation for EU accession, recognised the progress made by Latvia and encouraged the EU Commission to take this into account when presenting its Progress Report.

Since the beginning of the screening process in April 1998, the most significant sectors of the EU Internal Market have been screened. Latvia has been carefully preparing its participation in the screening process, which is an essential element of preparations for accession negotiations. The screening results have been analysed after each round and applied for use in further preparations for accession negotiations.

A free trade regime with the EU under the Europe Agreement has enhanced Latvia's economic capacity to cope with competitive pressures within the EU. The enhancements are visible using standard indicators. Exports have been growing consistently faster than GDP.

Despite a continuous appreciation of the national currency as compared to western currencies, the share of goods exported to western markets has been steadily growing. The EU has become the main trading partner for Latvia. In the first quarter of 1998, the share of trade with the EU in Latvia's total exports and imports grew to 52% and 54% respectively.

### **The Enhanced Pre-Accession Strategy**

For implementation of the Accession Partnership, on 28 March 1998 the Government adopted the Third National Programme for Integration into the European Union (the National Programme for the Adoption of the *acquis*). This document operationalises the priorities identified in the Accession Partnership and Latvia's obligations under the Europe Agreement, providing a timetable and describing resources for their implementation. The Programme covers the period from 1998 to 2002, and its implementation as well as compliance with the Europe Agreement will be regularly monitored and updated.

Latvia is using assistance provided through the EU PHARE programme and the Catch-up Facility and participating in Community programmes which enhance the effectiveness of efforts made in EU membership preparation.

## **B. CRITERIA FOR MEMBERSHIP**

### **1. Political Criteria**

#### **1.1. Democracy and the Rule of Law**

##### **The Parliament (*Saeima*)**

A number of important initiatives have been instituted by the Saeima over the past year: several amendments to the Constitution (*Satversme*) were adopted; a draft Chapter on Fundamental Human Rights is being discussed; the role of the European Affairs Committee has been strengthened. The opposition takes an active part in the work of the Saeima.

In December 1997, the Saeima adopted several amendments to the existing 1922 Constitution extending the term of the Saeima and the President from three to four years, reducing the time of parliamentary elections from two to one day, defining in a separate law the President's powers to pardon convicted criminals, and some further amendments.

Parliament's working group drafted a new Chapter of the Constitution on Fundamental Human Rights, which was accepted in the second reading.

The European Affairs Committee has proposed amendments to the Saeima's Rules of Procedure. These amendments are expected to be adopted in September 1998. This would create a common annotation system for all draft legislation submitted to the Saeima. This standard annotation form would provide Members of Saeima with information about the purpose of the proposed legislation, its potential impact on Latvia's economy and state budget, its compatibility with existing Latvia legislation (i.e. whether amendments are necessary to existing laws), its compatibility with Latvia's international obligations (especially with the *acquis communautaire*), and the manner in which the proposed legislation will be implemented (through existing or new government structures).

The European Affairs Committee monitors draft legislation for its compatibility with requirements of the Europe Agreement, as well as with the overall EU *acquis*. The Committee has also played a leading role in the adoption of significant new EU-compatible legislation in the areas of competition, state aid, money laundering and public utility regulation.

With assistance secured under the PHARE program, the European Affairs Committee is able to accomplish additional tasks, such as co-ordinating and organising a variety of training seminars on EU issues for MPs and parliamentary staff members, and to create an EU Information Centre at the Saeima. This PHARE assistance program specific for parliament is the only special program in Central and East Europe.

##### **The Executive**

Latvia is seriously working at improvement of the state administration capacities. The medium term strategy (Strategy 2000) and Action Plan for Public Administration Reform for the period 1998 - 2000 were adopted by the Cabinet in March 1998. The Prime Minister has assumed political leadership of public administration reform. In June 1997, a management system of public sector reform was re-established: the Council of Public Administration Reform is the policy-making body and the Bureau of Public Administration Reform is responsible for streamlining, modernisation of public administration and co-ordination of reform implementation.

In July 1998, the Government adopted a *Concept of the Development of the Civil Service System*. This measure was taken in order to clarify the institutional structure of public administration. Draft laws related to enhancements of the civil service have been submitted to the Government for approval. These include the draft laws *On Government Executive Agencies* and *On Administrative Procedures*. A substantial number of Latvian senior officials has been trained with an understanding of EU affairs both in Latvia and member states.

The Government has paid particular attention to improving the management and co-ordination of the EU integration process. The co-ordination of EU is developed with clear division of political and administrative responsibilities. The main decision-making governmental body - the European Integration Council (EIC) – is working under the leadership of the Prime Minister. The European Integration Bureau monitors the process by which Latvian legislation is brought into line with EU law, the harmonisation of legislation process.

Subordinated to the EIC, the Council of Senior Officials is the body responsible for inter-ministerial co-operation. The Ministry of Foreign Affairs is monitoring and co-ordinating the accession process and the Europe Agreement. Staff members responsible for EU policy implementation and co-ordination have been assigned and operate in each line ministry in close contact with the Ministry of Foreign Affairs.

Latvia participates in the EU Institution-Building program. An efficient co-ordination system for planning, programming and implementation of the institution building initiatives has been developed. A strategic institution building plan will have been drafted by September 1998.

In March 1998 the Government adopted a programme for prevention of corruption, which includes measures on prevention and enforcement, as well as education to the public.

Latvia continues to exercise civil control over the army, the secret services and the police. In June 1998, the Latvian Government decided to raise the state expenditure on defence to two percent of GDP within the next five years. It is planned to increase expenditures for the technical procurements and equipment for the army in the next year's state budget.

## **The Judicial System**

Reform of the judicial system has been continuing with an overall aim to strengthen the independence of the judiciary, to improve efficiency of the court system and to continue training of judges. A working group has been set up to draft a new law *On Judicial Power* for the codification of existing legal norms in this field.

Meanwhile, amendments to the existing law *On Judicial Power* (1992) and to the law *On the Disciplinary Liability of Judges* (1994) are scheduled for approval by the Saeima this year. Amendments provide that probation time for judges is extended from two to five years, and in exceptional cases for another two years. It is also envisaged that judges are no longer appointed to a specific court, but to courts of a certain level (district, regional, supreme). The positions of administrative judges in district (town) courts will be abolished since only minor differences exist in duties of administrative judges and district (town) judges. The increase of salaries by about 20% is envisaged for supreme court judges. An increase for other judges will be dependent of their qualifications.

In 1998, a comprehensive court computerisation project has been launched financed from the state budget. Preparation of connections of the National Data Transmission network, local court networks and the court office programme has begun. The project is scheduled to be implemented in the year of 2000.

The Constitutional Court was created in 1996. Amendments to the Law were adopted on 8 October 1997 with the aim of improving the court's operation. Ten court proceedings have taken place so far (6 cases in 1997, 4 in 1998), with sentences passed in 7 cases (2 cases in 1997; 5 in 1998).

On 3 March 1998 the Government approved the reform of the court bailiffs institution. Presently court bailiffs in Latvia are employees of the Department of Court Bailiffs, a unit of the Ministry of Justice. Court bailiffs will be transformed into a free legal profession. The Law *On Sworn Court Bailiffs* is being drafted. Latvian authorities are already receiving valuable bilateral assistance in these efforts and the reform of court bailiffs is also included in the PHARE project proposal for the continuation of judicial reform.

The training of judges in Latvia is organised by the Judicial Training Centre (JTC) which provides all judges and court staff with a regular qualification-raising opportunities. It also prepares relevant training programs, audio-visual materials and legal information. Since 1995, 320 judges and 325 court staff have been trained at the JTC. Additional training on the application of the EU *acquis* is envisaged.

Latvia plans to utilise PHARE support for the continuation of judicial reform, for the computerisation of courts, the preparation and implementation of laws *On Judicial Power*, *On Sworn Court Bailiffs*, as well as for training of judges.

### **1.2. Human Rights and the Protection of Minorities**

The Government continued its policy toward consolidation of society and further social integration. The Government's Programme for Integration of Society is being drafted and will be approved and released by October 1998. The fundamental human rights were guaranteed for all residents, minority rights were protected. The state provided assistance to minority cultural societies and financed education in eight minority languages. The implementation of the comprehensive Latvian language training programme continued. The number of naturalised persons has increased over the past year. The Law on Citizenship was further liberalised by the Saeima on 22 June 1998.

The Government conducted a constructive and open dialogue with the OSCE High Commissioner on National Minorities, the CBSS Commissioner, as well as with the United Nations, the Council of Europe and the

European Commission on matters related to the strengthening of democracy, rule of law and protection of human rights.

### **Civil and Political Rights**

In June 1997, Latvia ratified the European Convention for the Protection of Human Rights and Fundamental Freedoms (ECHR). Protocol No.6 of the ECHR concerning the abolition of the death penalty was accepted by the Government, signed on 26 June 1998 and forwarded to the Saeima for ratification.

During the first half of 1998, the number of naturalisation applications and consultations provided by the Naturalisation Board has significantly grown in comparison with previous years (from 12,000 in 1997 to 18,000 in 1998). As of 30 June 1998, 8,644 persons out of approximately 150,000 eligible have acquired citizenship through naturalisation.

In order to increase the pace of naturalisation and to implement a recommendation by the OSCE High Commissioner, in December 1997 the naturalisation fee for certain categories of applicants was reduced. Naturalisation test of Latvian history was simplified. More than 90 % of applicants successfully pass the tests in their first attempt, which suggests that requirements are reasonable. An information campaign has been initiated in order to increase the level knowledge on various aspects of naturalisation among possible applicants.

Further promoting the naturalisation process and implementing the OSCE recommendations, the Saeima on 22 June 1998 adopted amendments to the *Law On Citizenship*. These amendments :

- abolish the "windows" system that restricted application for naturalisation by age group;
- grants citizenship to stateless children born in Latvia after regaining of independence (21 August 1991);
- simplifies the naturalisation procedure for persons over 65 years of age.

Subsequently, a minority of the members of Parliament pushed for a referendum on the amendments, following a procedure prescribed in the Constitution. Thus the promulgation of amendments has been suspended for two months. If efforts to collect signatures for a referendum fail, promulgation of amendments can take place almost immediately.

Latvia's citizens and non-citizens enjoy the same fundamental human rights in accordance with the national and international law. Non-citizens are also under protection of the Republic of Latvia while travelling outside the country. Their travel is facilitated by the replacement of old Soviet passports with new non-citizens passport, which serves also as an official travel document. As of 16 July 1998, 241 354 non-citizens passports had been issued.

The law *On Refugees and Asylum Seekers*, adopted in June 1997, entered into force on 1 January 1998. The 1951 UN Convention on the Status of Refugees and its Protocol of 1967 was ratified without geographical restriction in October 1997. The Government closely co-operated with the UNHCR in these matters. Construction work of a Refugee Centre is continuing.

On 1 June 1998, the European Convention for the Prevention of Torture and Inhuman or Degrading Treatment or Punishment entered into force for Latvia.

Since 1994, Latvia has been reforming its prison system, establishing a system which comprises "closed", partially-closed and "open" prisons. Latvian penal institutions and facilities abide by recommendation R(87)3 of the Council of Europe. Further renovation of prisons was carried out to transform the cells previously housing a large number of inmates into smaller cells. Sports and rehabilitation facilities have been established in several prisons. Adolescents are accommodated separately from adults.

### **Economic, Social and Cultural Rights**

The *Avis* admits that the basic economic, social and cultural rights, as provided in international human rights instruments, are guaranteed in Latvia. Latvia works to ensure the implementation of these rights within the limitations which sometimes arise due to limited budgetary resources.

Latvia signed the "Social Charter" of the Council of Europe in 1997 and measures for its implementation have been instituted.

In 1998, there are 114 trade unions registered in Latvia. The National Human Rights Office of Latvia completed a study on the Situation of Economic and Social Rights in Latvia in April 1998. The report focuses on problems connected with poverty, social security and social insurance. It also contains recommendations for the Government's policies in these matters.

The Ministry of Welfare is working on the project "Poverty in Latvia" in co-operation with the UNDP and the World Bank. The report will be followed by recommendations which will serve as a basis for the Government's national policy.

The issue of differences between citizens and non-citizens in their right to practise certain professions remains under consideration in the Saeima. There are no OSCE recommendations on this issue. Differences which existed related to the occupation of fire-fighters, aircraft crew members, pharmacists, and veterinary pharmacists have been abolished.

According to the legislation of the Republic of Latvia, the economic and social rights of citizens and non-citizens are principally the same. The law *On the Rights and Obligations of a Citizen and a Person* (1991) guarantees the equality of all inhabitants of Latvia, as well as granting *inter alia* the following rights: the right to own property, the right to work, the right to freedom of movement and the right to education.

## **Minority Rights and the Protection of Minorities**

Latvian legislation guarantees the rights of national minorities in the spheres of language and culture and the Government provides financial support for their development. The state renders assistance and support to minority cultural societies and state-financed education is available in eight languages besides Latvian.

In order to promote integration of society, on 31 March 1998 the Prime Minister established a ministerial-level Integration Council. The Council has been instructed to draft a National Programme for Integration of Society by October 1998. During the drafting process the Council is taking note of a large-scale research project *On the Way to Civic Society* (published in March 1998). The research project was carried out by the Naturalisation Board with the assistance of the National Human Rights Office, the Citizenship and Migration Affairs Agency of the Ministry of Interior, the Ministry of Education and Science, the Institute of Philosophy and Sociology, the OSCE Mission in Latvia and the Soros Foundation.

Integration of society is further promoted through Latvian language instruction. The Government of Latvia, in co-operation with the UNDP, is implementing the multi-donor project, the "National Programme for Latvian Language Training for the non-Latvian speaking population". The first phase of the project will end in December 1998. During the first phase the core group of teachers for Latvian language education will have received essential training. New textbooks for students of Latvian and handbooks for teachers have been prepared. Videos for learning Latvian have also been developed. The project will be expanded during the next two years and will focus on support for operational delivery of language training and development of managerial and implementation capacities to sustain the National Programme beyond the term of the project. A total sum of USD 3,220,000 has been provided by multilateral and bilateral donors, including USD 700,000 from the EU for the period 1996-98.

## **2. Economic Criteria**

### **2.1. The Economy in the Perspective Member State**

During the pre-accession period, achieving macroeconomic stability and ensuring economic growth are as important as harmonisation of legislation. One of the most important tasks for the Government is to promote sustainable economic growth in the country so that the gap between Latvia's economic development and that of the EU is diminished. Latvia is one of a few applicant states which adopted the Medium-term Economic Strategy in the Context of Accession to the EU.

### **Recent Macroeconomic Indicators and Structural Adjustments**

1997 and the first half of 1998 were successful for the Latvian economy. Industrial output increased significantly; the inflation rate declined more rapidly than had been forecasted and fell to single digits. Despite an increase in the current account deficit, foreign reserves increased. The country's budget performance in 1997 was commendable because Latvia managed to implement the intended balanced budget policy. Fiscal surplus amounted to 1.3% of the Gross Domestic Product (GDP). The Latvia's financial indicators meet the requirements of the Maastricht treaty with respect to the budget deficit, government debt, and exchange rate stability.

The positive development of Latvia's economy has been acknowledged by international credit rating agencies. Standard & Poor's gave Latvia a 'BBB' rating for long-term loans in foreign currency and an 'A-' rating for long-term loans in the national currency, while Moody's gave Latvia a rating of 'Baa2' for long-term credits (a rating which corresponds to Standard & Poor's 'BBB' category). Fitch IBCA also ranked Latvia in the 'investment country' category. These ratings are among the highest in Central and Eastern Europe.

### Real Sector

The economy has grown substantially. GDP growth in 1997 amounted to 6.5%. In the first quarter of 1998, GDP growth was 7.6% when compared to the same period the previous year. The growth was export and investment-driven. A surge in foreign direct investment (FDI) and domestic credit was observed. While GDP growth in 1996 was fostered mainly by success in the transport and service sector, in 1997 growth was achieved in virtually all sectors of the economy.

Development of processing industries is represented by positive indicators. The growth of manufacturing reached 7.0% in 1997 and 13.6% in the first quarter of 1998 in comparison to the same period the previous year. In 1997, the agriculture and forestry sector experienced 4.9% growth.

Uneven rates of growth in different sectors of the economy resulted in significant changes in the distribution of GDP by sector.

The service sector share of the total value-added continued to increase, reaching 61.9% in 1997. The transport and communication branch is dominant in the service sector. At the same time, the agriculture share dropped to 7.4%, while industry stabilised at 21% of the total volume of value-added.

The growth rate of Consumer Price Index (CPI) in Latvia is persistently slowing down. Diminishing inflation is one of the main long-term goals of the Government's economic policies. In 1997, compared to the previous year, CPI amounted to 8.4%. 12-month inflation in May 1998 was 5.4%.

The official unemployment rate has stabilised at around 7.0% of economically active residents. While industrial restructuring and modernisation caused losses in various sectors of the economy, this was apparently compensated by intensifying economic activity and gains in employment within SMEs.

### Balance of Payments

The current account deficit in the balance of payments amounted to 6.3% of GDP in 1997. This is an usual phenomenon for a country where natural resources are scarce and where an urgent need for modern equipment and technologies persists due to transition. Imports are dominated by machinery, equipment and electrical equipment (19%), followed by mineral products (14%), and metals and metal products (8%). Ongoing restructuring demands considerable inputs of resources. This is reflected by a constantly increasing share of investment goods in imports.

Strong growth in the exports of goods and services has continued (a 9.9% increase in 1997). The main export products are wood and wood products; these comprise approximately one third of total exports, textiles and textile products (16%), machinery and equipment (9%), and electrical equipment and metal and metal products (9%). Although there have been no radical changes in the general export structure, a stable trend towards exporting products with a higher added value is being observed within the above-mentioned product categories.

A substantial surplus in the capital account entirely covers the large deficit on the current account. FDI inflows resulted in coverage of approximately 94.7 % of the current account deficit. A positive fact is that Latvia is a creditor concerning short-term capital positions and a debtor in respect to long-term capital positions. Even though the current account was negative, the over-all balance of payments was positive.

With regard to large foreign capital inflow or outflow, the Bank of Latvia will be ready to intervene in the foreign exchange market in order to control inflows, or to protect the exchange rate of the LVL in case of sudden outflows. The Bank of Latvia possesses sufficient foreign exchange reserves and has developed adequate monetary policy instruments to cope with unexpected capital flows into or out of Latvia.

### Public Finance

Since the beginning of transition, the Government has implemented a strict fiscal policy through a major revenue mobilisation effort combined with expenditure restraint. As a result of stronger-than-expected economic growth and improved tax collection, a fiscal surplus of 1.3% was recorded in 1997. The Medium-term Economic Strategy aims at restricting possible fiscal deficit to 0.5% of GDP in the coming years.

Over the last two years tax revenues have been growing more rapidly than GDP, pointing to significant improvements in tax administration. Reorganisation of the State Revenue Service and setting tax revenue targets for regional units significantly contributed to tax revenue growth. Tax volumes collected at customs check-points increased mainly as a result of improved handling of goods and processing of customs documents, as well as improved control procedures.

Tax arrears had been declining during 1997. On 1 January 1998, the State Revenue Service assumed responsibility for collecting social insurance contributions. This should result in increased collections in this area over the medium term.

To promote more effective allocation of budget resources, since 1997 budget expenditure has been planned according to budget programs and sub-programs. Increased control over the borrowing of local governments, as well as incorporation of all extra-budgetary funds into the treasury, greatly contributed to more efficient budget management. In 1997, management of the external debt was enhanced by inclusion of all loan agreements and credit guarantees in the annual budget law. The state's goal of increasing public investment is being achieved through improving expenditure management. Priority sectors for investment are energy, transport and environmental protection.

### Financial sector

1998 is the third consecutive year marked by stable and controlled growth in the banking sector. Banks have strengthened their capital base, a noticeable shift towards more lending to the real economy has taken place and the gap between deposit and lending rates has narrowed. Expansion in domestic lending is accompanied by a stable decrease of non-performing loans portfolios both in relative and absolute terms. By the end of March 1998, the share of non-performing loans (i.e., loans that require provisions against possible losses) has decreased to 8%; in this category, 4% are "bad" loans. At the end of 1996, these figures were 20% and 13% respectively. The loss provision scheme in Latvia is rather tight and is strictly enforced, so the non-performing loans do not pose any threat to the stability of the banking sector.

Strengthening of the banking sector undoubtedly contributed to Latvia's strong macroeconomic performance in 1997 – 1998. Conversely, positive developments in the real economy, as well as favourable macroeconomic conditions created new opportunities for the banking industry.

The number of commercial banks in Latvia has seen gradually decreasing from thirty five in January 1997 to thirty one in July 1998; this figure includes the branches and subsidiaries of foreign banks. The share of private capital in the banking sector has reached 95%. Foreign ownership grew to 63%.

By 31 May 1998, total assets of the banking sector reached LVL 1.8 billion (compared to LVL 1.1 billion at the end of 1996), and total equity LVL 226 million (LVL 149 million at the end of 1996).

All banks have reached the minimum capital level (LVL 2 million as of 1 April 1998) as stipulated by the law. Further consolidation of the banking sector is taking place (the assets of 4 major banks compose approximately 50% of the total assets in the banking sector and 72% of assets are currently concentrated in 9 major banks).

Bank lending has increased by 74% in 1997 and a further increase of 19% has been recorded in the first quarter of 1998. 94% of credits are issued to the private sector, and residents of Latvia receive 75% of total credits. Commercial banks expanded their long-term crediting programs to businesses. Nominal and real interest rates declined rapidly from the beginning of 1997, reflecting fiscal narrowing, constantly falling inflation and the favourable credit ratings which were awarded to Latvia.

The refinancing rate was reduced to 4%. Interbank credit rates have ranged between 3% and 5% since January 1997. By the end of 1997 the average weighted interest rate on long-term credits issued by commercial banks in LVL declined to 13.3%, while the rate on short-term credits fell to 12.2%.

Over the last years, the necessary arrangements to complete creation of an efficient and liquid securities market in Latvia have been undertaken. The Riga Stock Exchange, the Central Depository of Latvia and the Securities Market Commission form a proper institutional framework for efficient operation of the capital market.

Taking into account the scheduled privatisation of the biggest monopoly companies, volume of the securities market is projected to reach a level of USD 2.5 billion by the end of 1999. Private companies are also becoming more active where their transformation into public joint stock companies is concerned. Recently, instruments such as derivatives (call and put options) appeared on the market. By September 1998, brokerage companies must reach a LVL 100,000 capital requirement. Furthermore, new requirements to brokerage companies based on provisions of the capital adequacy directive are being drafted to become effective in the year 2000.

The insurance market grew from 1% of GDP in 1993 to 2% in 1997 and this trend is continuing. For example, in the non-life insurance sector the volume of written premiums has increased by 140% during the first five months of 1998, compared to the same period in 1997. One of the reasons for this is the introduction of compulsory third party liability insurance for motor vehicle owners in 1997. The life insurance sector is also increasing, albeit at a slower rate. There is a gradual tendency for the number of insurance companies to decrease. In 1997, the privatisation process of the single state-owned insurance company was almost completed. The insurance market in Latvia is being effectively supervised by the State Insurance Supervision Inspectorate.

## The Existence of a Functioning Market Economy

Recent steps made by Latvia in the area of economic reforms have completed the establishment of a functioning market economy.

As a result of consistent government policy and action, the private sector accounted for 62% of GDP and employed 66% of the country's workforce by the end of 1997. In such important sectors as manufacturing, agriculture, construction and trade, companies controlled by private owners contribute between 90% and 98% of the gross value added in these sectors.

The privatisation process in Latvia is almost completed. By mid-1998 nearly 95% of the former state-owned enterprises were privatised. Sectoral strategies for specific areas where privatisation is complicated, such as public utilities, have been elaborated. The state's share in public utilities is being constantly decreased. By the end of April 1998, private ownership of "Ventspils Nafta" (a major oil transit company) had grown to 51%. The rules covering the decrease of the state's share in the Latvian Gas Company to less than 50% by the end of 1998 were accepted in May. The fact that the utilities sector is still dominated by the state does not pose a serious obstacle for the overall economic development since restructuring and modernisation of this sector are constantly being promoted. Despite the upcoming parliamentary elections and related discussions on whether it is necessary to privatise strategically important enterprises, the Government is firmly committed to fulfilling the privatisation steps envisaged in the National Programme for Integration in the EU.

The Government's commitment towards pursuing liberal economic policies has been reinforced by recent developments. The import duty on raw materials and manufactured articles which are not produced in Latvia has been abolished. This regards commodity groups such as machines and equipment, transport vehicles, chemical products, medical goods and optics. By the end of 1998 the export tax on wood materials is to be abolished and the average production weighted customs duty on agricultural products will not exceed 30%, once amendments to the law *On Customs Tariffs* has been adopted.

The number of types of activities which require a license decreased from 165 to 67 in 1997. The process of liberalisation includes establishing free trade relations (at present, Latvia has free trade relations with 26 countries including the EU member states), and trade with 21 other countries is regulated by bilateral trade agreements).

Liberalisation of the land market was completed in May 1997. The land and property register is still being developed. The reform of Land Books carried out in the framework of PHARE technical assistance project is going to be accomplished. The process of settling restitution claims and the registration of land is advancing and almost all properties are now registered in the Land Book. At the end of 1997, 130,000 units were registered in the Land Book. This number should increase to 200,000 by the end of 1998.

The Government has made efforts to ensure that legislation was comprehensive and transparent. Reforming the tax system according to the requirements of the market economy provided a sound environment for both local and foreign businesses that is an inseparable component of the market economy. A new *Customs Law* which corresponds to the EU requirements and promotes trade while ensuring proper tax collection became effective in July 1997.

In 1997, distortions of competition in the field of public procurement were removed. The existing legislative base for free competition in Latvia was reinforced by the new *Competition Law* which became effective on 1 January 1998, and also by the law *On State Aid Control* which came into force in March 1998.

The strong and rapidly growing financial sector including capital market, banking business and insurance is fully supportive for successful functioning of the market economy in Latvia. The regulatory framework for the financial sector has been harmonised with EU regulations (see chapter 3.1). A system of collateral register has been refined, thus facilitating access to credit resources. Recent adoption of the legislation package on investment companies and mortgage bonds will greatly add to successful performance in the financial sector.

In order to facilitate the process of registration of enterprises, to protect entrepreneurs and to bring Latvia's legislation closer to EU legislation, a new Commercial Code is being prepared. The new Commercial Code and amendments to existing regulations will encompass eight EU directives and norms in the area of company law, accounting and civil matters. This law package is expected to come in force at the beginning of 1999. Together with the revised Civil Code of 1937 and the newly adopted Criminal Code of 1998, the Commercial Code will provide the basis for a modern Commercial Law in theory and in practice.

The registration of enterprises is carried out by the Enterprise Register, which has a high level of computerisation and technical equipment. The Enterprise Register is preparing to join the European Business Register. Since February 1998 when the Commercial Pledges Register was created, more than 1200 records for the total amount of LVL 463.5 million have been registered thereby enhancing the stability of economic relations.

## **The Capacity to Cope with Competitive Pressure and Market Forces**

The structure of export is improving. The share of processing industries in total export is increasing between 1995 and 1997 from 85% to 93%. The quality of export is upgrading and export with a relatively high value added is increasing. In 1997, the biggest increase in export was noted in the following products of the processing industry: wood and articles of wood (49%), textiles (13%), prepared foodstuffs (5%), products of chemical and allied industries (20%), machinery and mechanical appliances (14%). In the largest category, in export of wood and articles of wood, instead of the massive export of round timber in 1993 - 1995, the export of saw materials is increasing constantly.

The share of services in export remains considerable (30%). On transit transport Latvia enjoys a very favourable situation with her two big ice free ports of Ventspils and Liepaja, and the pipelines and railways from there to Russia. During 1995 - 97 the turnover of Latvian ports increased by nearly 1/3 to 51 million tons, and the railway transit haulage increased by nearly 50% to 31 million tons. During 1997 28 1/2 million tons of oil were transmitted through Latvia's railways, pipelines and ports. In the first quarter of 1998, there was anew an increase in export of transport services. The ports of Ventspils and Liepaja are being upgraded, and the transport system is technically able to cope with the requirements of the coming years. The export of financial, communication, computer and information and other business services also increased.

Improved capacity of the Latvia's economy to cope with competitive pressure and market forces is testified to by favourable macroeconomic evidence.

A free trade regime with the EU under the Free Trade Agreement and subsequently under the Europe Agreement enables Latvian companies to prepare for competition within the EU. Traditional indicators describing external competitiveness reflect that the capacity of Latvia's economy to cope with competitive pressure and market forces within the EU has been enhanced. Exports have been growing consistently faster than GDP. Exports growth rates are high, with no signs of a marked slowdown. Despite a continuous real appreciation of the national currency towards the western currencies, the share of goods exported to the western markets has regularly been growing faster than that to the eastern markets. The EU has become the main trading partner of Latvia. At the end of 1997, Latvia's exports and imports to the EU comprised 49% and 53% of total exports and imports respectively, while in the first quarter of 1998, the EU share in Latvia's total exports and imports grew to 52.0% and 54.1% respectively.

Cumulative data for the last two years reflect the fact that productivity has been growing much faster than wages (real after-tax wages increased by 1.6% while growth in average productivity reached 11.1 %).

Restructuring of the economy was fuelled by growing volumes of FDI inflows. In 1997, these were especially abundant, amounting to 9.4% of GDP. The growth rate of foreign investments in Latvia in 1997 was higher than that in the other Baltic states. Withdrawal of the Government as a major borrower from the commercial banking sector has allowed a rapid increase in lending to the private sector and has helped in the reduction of commercial lending rates. Gross fixed capital formation increased by 11.1% at constant prices in 1997.

The macroeconomic environment in Latvia has become so stable that an individual economic actors can make decisions in a reasonably predictable climate. The competitiveness of the Latvia's economy is further enhanced by the Government's consistent policy measures.

Recognising that introduction and implementation of quality standards is important for assuring competitiveness of producers in domestic and foreign markets and in order to remove technical barriers for exports, issues related to quality of products and standards are thoroughly reviewed under the National Quality Programme, the Standardisation Programme and the Market Surveillance (supervision) Programme.

Amendments to existing legislation are being prepared to ensure conformity with EU requirements on quality issues. At present, 200 EU standards have been introduced. The full implementation of EU standards is expected by 2002. The institutional framework is being reinforced.

Integration of the Baltic financial markets is being continued. It is widely recognised that separately the Baltic securities markets will not be able to endure competitive pressure in the European context, therefore integration of the Baltic securities market in the short term and then their integration in European securities market in the longer term are considered to be one of the top policy priorities.

As a result of progressive macroeconomic development, a strengthened financial sector and legislative improvements, companies now have easier access to financial resources necessary for restructuring which, in turn, improves the ability to cope with competitive pressures and market forces in the EU.

### 3. Ability to assume the obligations of membership.

#### 3.1 Internal Market Without Frontiers

##### The Four Freedoms

###### **General Framework**

This year, February 1st, the Europe Agreement between Latvia and EU entered into force. The Agreement provides guidelines for gradual implementation of the four freedoms and approximation of legislation. The obligations that follow from Latvia's participation in the single market is a test of Latvia's ability to manage the double task of simultaneously creating a modern and coherent legal system and implementing the EU legislation, its system and "*effet utile*". The political and administrative system of Latvia has proved effective in executing tasks in accordance with the Third National Program for Adoption of the *acquis*, and the simultaneous work on EU and Latvian legislation has meant that we arrive without deviation at a modern legislative acts. As mentioned under 2.1, two important examples of this are the draft *Commercial Code* and *Competition Law*.

Regarding the implementation of framework directives necessary for regulating a market economy significant progress has been made. Latvia has already established liberal price, trade and foreign exchange regime. Considerable progress has been achieved in the areas of standardisation and quality control, intellectual property rights, competition, etc. It is expected that most of the *acquis* related to the free movement of goods will be implemented by the end of 1999.

Completion of liberalisation of the land market can be considered as the last step in eliminating restrictions on capital movement.

1998 is the third consecutive year marked by stable and controlled growth in the banking sector. Also insurance and securities markets are developing. During the last years so many efforts have been devoted to perfecting financial services legislation and strengthening the applicable supervisory structures that further development of the sector depends mostly on the overall economic development.

Tight control of compliance with the EU rules of public procurement is one of the top priorities for the Government of Latvia. The existing public procurement rules will be extended to the utilities sector. Latvia intends to become a Contracting Party to the WTO Agreement on Government Procurement by year 2000.

The law *On Public and Municipal Procurement* which came into effect on 1 January 1997, was reinforced by a number of secondary regulations. Adoption of a draft law *On Works, Supplies and Services Procured by the Utilities Sector* is expected in mid-1999. The draft law provides for an independent review body (even now any participant of the tender has a possibility to sue the procuring entity in court if there are doubts about legality of tender results). The regulations in force containing provisions on procedures of tenders and services are in accordance with EU requirements

National legislation in the area of competition and state aid control was adopted and a state aid control institution was established in accordance with EU requirements. Latvia is the first of the associated states to have a fully functioning state aid control system.

Regarding intellectual and industrial property rights, considerable progress has been achieved. Latvia is a member of the Berne Convention on Protection of Literary and Artistic Works since 1995 and the Geneva Convention for the Protection of Producers of Phonograms Against Unauthorised Duplication of Their Phonograms since 1997. In March 1998, the Saeima passed the law joining the Rome Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organisations. The law will be in force from 1 January 1999.

Latvia will join the WIPO Copyright Treaty and WIPO Performances and Phonograms Treaty before the end of 1998.

Upon accession to the WTO (expected in Autumn 1998) Latvia will join the TRIPS agreement. Already, full compliance with the TRIPS requirements has been ensured.

At the moment, active work is taking place on further accession to conventions in the field of industrial property. For example, draft laws on accession to the Madrid Agreement on the International Register of Trademarks and related Protocol have been submitted to the Saeima for consideration.

It is foreseen that by the end of 1998 a new law *On Copyright and Neighbouring Rights* and relevant regulations will be adopted and come into effect: *On Measures of Customs Authorities for the Protection of Intellectual Property*, *On Distribution of Sound Recordings, Films and CD ROM's*, and *On Trade in Markets*,

*Drive Markets and on Streets*. Amendments to the *Administrative Offences Code* on illegal distribution of neighbouring rights to a work and the use of copyrighted work without a licence are currently passing through legislative procedures in the Saeima. The new Criminal Code, passed in July 1998, contains provisions of criminal responsibility for infringement of copyright and illegal use copyrighted work and neighbouring rights.

A new draft law *On Trademarks and Instructions of Geographical Origin* (submitted to the Saeima) fully conforms to the relevant Directive. The law *On the Legal Protection of Topographies of Semi-conductor Products* (in force since April 1998) is harmonised with the corresponding Directive.

The Third National Program for European Integration includes the question of establishment of state institutions. A Copyright and Neighbouring Rights Division for dealing with copyright and neighbouring rights should start operating in the Ministry of Culture in February 1999.

In order to improve the theoretical and practical knowledge of police, customs, prosecutors and judges, different programs have been organized in co-operation with PHARE. In early 1998, the Handbook on Copyright was published to popularise and explain the meaning of copyright and to give practical assistance for authors, users of their works and lawyers.

Implementation of the EU requirements in accounting is being steadily accomplished. A separate law on consolidated accounts will be adopted before July, 1999. The transposition of international accounting standards in the banking sector has already been completed. Special attention is being paid to educating auditors and accountants. The Latvian Association of Sworn Auditors established its own Educational Centre which is organising courses on accounting and auditing in co-operation with international institutions and PHARE. In the future, it is planned to expand these educational activities and cover also regional centres.

The draft Law *On Personal Data Protection* is submitted to the Saeima.

So by the end of 1998, the legislative and institutional frameworks in Latvia will have structures and contents that are both in conformity with the *acquis* and the requirements of a modern market economy.

### **Free Movement of Goods**

Since June 1997 considerable progress has been achieved as far as freedom in the movement of goods. The relevant horizontal legislation has already been adopted and sector legislation is being drafted. All quantitative import restrictions are eliminated. As already mentioned in previous section, it is expected that the legislation related to the free movement of goods will be implemented by the end of 1999.

A new draft law *On Standardisation* will be adopted in Autumn 1998. The Government approved *The Standardisation Development Program*, which forms the basis for the adoption of all European standards before the end of 2004. More than two hundred European standards in the different fields have been adopted so far.

The principles of Decision 3052/95 on measures derogating from the principle of free movement of goods will be introduced into national legislation during 1999.

A regulation *On the Conformity Assessment Modules in Mandatory Area* has been approved. The regulation provides guidance for use of European CE marking and general requirements of the New Approach modules for conformity assessment and conformity assessment procedures. Essential requirements of the directives on electrical safety and electromagnetic compatibility of apparatus have been incorporated into two regulations of the Government of April and May 1998. The Regulation *On the Conformity Assessment for Construction Products* of August 1997 fully corresponds to the requirements of the EU. It is expected that regulation *On Machinery Safety* and regulation *On Personal Protective Equipment* will be adopted before the end of 1998. Legislation on motor vehicles will be implemented before the end of 1999.

Most of the requirements of EU directives concerning foodstuffs have been implemented. The Law *On the Surveillance of Food Circulation*, adopted in February 1998, provides for the implementation of EU directives concerning food control and food hygiene. Several regulations of the Government have been accepted in areas such as products and articles coming into contact with foodstuffs, hygiene of fishery products, hygiene of food enterprises, solvents for use in food production, veterinary requirements for slaughtering of animals, control of radioactive contamination, and labelling of foodstuffs.

The new law *On Chemical Substances and Chemical Products* was adopted in April 1998. The following regulations will be prepared by the end of 1998: *On the Classification, Packaging and Labelling of Chemical Substances and Chemical Products*; *On the Limitation of the Use and Trade of Dangerous Chemical Substances and Dangerous Chemical Products*; *On the Limitations of the Import and Export of Certain Chemical Substances*; *On the Security Data Sheets*.

A new law *On Pharmaceutical Activities* incorporates the relevant provisions of EU legislation. The regulations *On the Registration of Medicinal Products; On Classification of Medicinal Products for Human Use; On the Labelling of Medicinal Products and Package Leaflets* have been adopted.

The regulation *On the Creation of Supplementary Protection Certificates for Plant Protection Products* will be implemented after the entering into force of the Law *On Plant Protection* at the end of 1999.

### ***Free Movement of Capital***

Latvia has one of the most liberal regimes for movement of capital in the world. No restrictions on convertibility of national currency exist in Latvia both in respect to the current account and capital account transactions. Foreign investors can freely repatriate their investments and profits after paying the taxes due. Almost all financial transactions mentioned in the Directive 88/361 are free.

An upswing of foreign direct investments was to a large extent stimulated by elimination of almost all remaining restrictions on foreign investment and notification requirements in early 1996, as well as by abolition of restrictions for participation in the privatisation certificate market.

Currently, restrictions on foreign direct investment inflow in Latvia remain only in 3 branches of the economy - the logging industry, the radio and TV industry and lottery and gambling industry. Nevertheless, foreigners may own up to 49% of companies in these sectors.

Liberalisation of the land market was completed in May 1997. No restrictions exist for the purchase of buildings. There are no restrictions to transactions in securities.

The basic principles of investor protection in Latvia are laid down by the law *On Foreign Investment in the Republic of Latvia*. Latvia has signed investment promotion and protection agreements with all the EU member states except Ireland. Latvia has begun preparations for joining the OECD Multilateral Agreement on Investment and amendments to the draft reservation list are being prepared, taking into account the results of consultations with the European Commission.

### ***Free Movement of Services***

In Latvia, the overall objective is to develop the financial sector in such a way that it could contribute to economic development through an effective allocation of resources, ensure the proper level of protection of investors, depositors and the insured comparable to that in EU Member States. Furthermore, the Government aims to promote eventual consolidation of supervising authorities of the financial market. Further development of this sector depends mainly on successful performance of the real sector.

Overall strengthening of the banking sector in 1997–98 was driven mainly by the market forces, and efforts of the Latvian authorities to improve legislation. In addition to the previously implemented directives, during 1997 and first half of 1998, Latvia undertook serious measures in order to accomplish legislative harmonisation in the banking sector.

The law *On Prevention of Use of the Financial System for the Purpose of Money Laundering* took effect from 1 June 1998. The law *On Deposit Guarantees* will come into force as of October 1, 1998. While initially insuring deposits of physical persons only up to a modest amount of 770 ECU, the law includes a timetable for attaining the 20,000 ECU level determined by the respective EU directive.

Amendments to the law *On Credit Institutions* were passed by the Saeima in May, 1998, setting improved procedures for bankruptcy, liquidation and rehabilitation of credit institutions. The aforementioned amendments also establish a legal basis for the introduction of consolidated supervision of credit institutions in 1999. In addition, the amendments to the law *On Credit Institutions* enable the supervisory authority to exchange information required for implementation of consolidated supervision with other supervisory institutions, both domestic and foreign. Bank of Latvia will prepare the necessary regulatory framework for compliance with the directive on *Annual Accounts and Consolidated Accounts* by the end of 1998, and the directive will be fully implemented during 1999. Full implementation of the *Capital Adequacy* directive is scheduled for the end of 1999.

Banks are successfully complying with gradually increasing capital requirements. By the end of 1999 all banks will have to reach a 5 million ECU capital level. The Central Bank is closely following the situation in the banking sector. Due to inability to reach the required minimum capital three banks lost their licenses since January 1997.

In general, the number of restrictions imposed on banks is decreasing, reflecting an improved performance in the banking sector. During 1997 and first half of 1998, 199 on-site inspections were performed. Taking into

account significant improvement of the quality of analysis and skill of the supervisory staff, the Bank of Latvia is gradually shifting towards off-site analysis.

A sound institutional and legal framework for development of the securities market has been created. The Securities Market Commission - an independent supervisory body - was established at the end of 1996 and currently employs 23 persons. Since 1997, 12 licenses of legal entities and 362 of individuals (brokers) were granted. During this period, the Securities Market Commission carried out 69 inspections in banks and brokerage companies.

In 1997, transposition of first stage directives in the securities field has been completed. Presently, the requirements to brokerage companies in the field of capital adequacy are being revised on the basis of EU Directive *On the Capital Adequacy for Investments Firms and Credit Institutions*. These are expected to be adopted by the year 2000.

Looking through the new legislation in the securities field, one notices that the law *On Investment Companies* came into force in 1 July 1998 and the regulation *On Mortgage Bonds* in April, 1998. As for the mortgage bonds regulations, a positive aspect of the manner of application is the choice of a non-discriminatory approach: any bank meeting certain prudential norms (e.g. capital requirements) is able to receive permission to issue mortgage bonds.

The trading system of the Riga Stock Exchange (RSE) has been developed considerably during last years. Trading at the RSE is continuous, order-driven, centralised and fully computerised. There are three lists at the RSE: official, second and free. Actually requirements for admission to official listing are higher than those requested by EU. Both local and foreign issuers may be listed, and they will have the same requirements. Settlements among members of the RSE are implemented through the Latvian Central Depository (LCD) on a delivery-versus-payment basis. As a result of co-operation with international institutions the LCD introduced advanced technologies and started a project of Securities Lending/Borrowing Program. Real time gross settlement, link with payment system, cross-border settlement development were implemented on the basis of the European Central Securities Depositories Association recommendations. The LCD has co-operation agreement with the Estonian Central Depository for Securities. Currently the LCD plans to establish a similar link with the Lithuanian market. The LCD provides registration, distribution and settlement for securities issued in Latvia by foreign issuers.

On 1 September 1998, new laws in the insurance field - the law *On Insurance Contracts* dealing with private law norms and the law *On Insurance Companies and Their Supervision* dealing with public law norms - will come into force. As a result a special fund for protection of the insured will be established, the notion of insurance broker companies and a guarantee fund will be introduced, a more detailed regulatory framework will govern investment made by insurance companies and higher requirements will apply to mutual insurance associations.

Cancellation of the prohibition for foreign insurance companies to establish branches in Latvia is scheduled for 2003 (presently they are allowed to establish their subsidiaries).

The law *On Compulsory Insurance for Inland Motor Vehicles Owners* came into force in September 1997. The Traffic Bureau of Latvia was admitted to the Green Card System as a "Transitional Member" as of 1 July 1998. It is expected that Latvian Green Cards will come into circulation in October-November 1998.

A new field of activity for the State Insurance Supervision Inspectorate (SISI) is supervision of private pension funds. The relevant law came into force on 1 July 1998. SISI has remarkably developed its professional capacity thus ensuring a proper protection for clients of insurance companies. SISI favours a method of preventive supervision aiming at discovering possible problems at an early stage. During 1997 and the first half of 1998, licenses of 2 insurance companies were annulled due to their failure to comply with prudential requirements. Since 1996 there were no insolvency cases where the clients of insurance companies would have suffered. At the moment, SISI staff consists of 22 qualified employees (19 - at the end of 1997). SISI regularly performs both general and topical inspections.

A key element in the supervision strategy of the financial market is the establishment of a single financial market (banking, insurance and securities market) supervisory authority. This proposal was generally adopted by the Government on 20 June 1998.

Concerning the opening of national markets in the sectors traditionally dominated by monopolies, this year Latvia began a comprehensive reform in the telecommunications sector in order to achieve full liberalisation by 1 January 2003 and to create a telecommunications regulatory environment in line with EU directives (see Telecommunications). Comprehensive work has been done to integrate the energy sector into the EU internal market, to develop competition and the energy market (see Energy) as well as to improve the quality and competitiveness of services in transport sector (see Transport).

## **Free Movement of Persons**

### *(a) Free Movement of Union Citizens; Freedom of Establishment and Mutual Recognition of Diplomas and Qualifications*

The draft law *On Regulated Professions and Recognition of Professional Qualifications* comprising fundamental norms in the field of mutual recognition of professional qualifications included in the Treaty of Rome, the two general directives and the sectoral directives, as well as the lists of professions included in 37 so-called liberalisation and transitional directives, is expected to be submitted to the new Saeima by the end of 1998.

It is anticipated that by 2003 all Latvian higher education programs will be compatible with those of EU Member States (including implementation of sectoral directives concerning mutual recognition of professional qualifications - see "Education, Training and Youth").

Co-ordination in the field of social security is fostered by bilateral agreements. Currently Latvia has concluded relevant agreements with Lithuania, Estonia and the Ukraine (signed, but not in force) on social security, with the USA on export of pensions and with Sweden on medical care for temporary visitors (in force since 1 May 1998). It is expected that an agreement on social security will be signed with Finland this year.

A regulation *On Employment Procedure for Foreigners and Stateless Persons in the Republic of Latvia* was adopted in February 1998. The legislation in Latvia does not discriminate against legally employed foreigners and stateless persons.

The provisions of the EC Regulation 1408/71 will be implemented by the State Social Insurance Agency and the State Health Insurance Central Fund.

The consequences for the legislation in Latvia of the rules giving citizens and companies the right of establishment and of performing services are currently being analysed, both on the general level and in relation to the various trades and professions. The analysis is expected in the beginning of 1999.

### *(b) Abolition of checks on persons at internal frontiers*

Latvia is taking an active steps to fulfil the provisions of the Schengen *acquis* after the year 2000.

A computerised system for visa identification and registration has been prepared for implementation by the Latvian authorities with the assistance of international expertise. The participants of the Baltic consular service consultations in January 1998 agreed on the necessity to introduce a joint information system based on the model of the Schengen information system. This would increase the effectiveness of cooperation in migration control and issuing of entry documents (visas and residence permits), with a view to the Baltic States entering the EU visa space as a united visa space themselves.

Since January 1997 bilateral visa-free regimes have entered into force between Latvia and Andorra, Denmark, Ireland, Liechtenstein, Malta, Norway, Finland, Switzerland and Sweden. Agreement on visa regime abolition have been signed with Slovenia.

Amendments to the law *On the Entry and Residence of Foreign Citizens and Stateless Persons in the Republic of Latvia* have been made whereby a visa-free regime has been adopted for carriers of European Commission passports and EU member state diplomatic and service passports.

In order to improve security of citizen passports a special working group has been established and a tender for designing of the new passport will be published by 1 September 1998. The results of the tender will be evaluated and submitted to the Government by 31 December 1998.

Since July 1997 Latvia has concluded agreements on the readmission of persons residing illegally with France, Italy, Liechtenstein, Norway, Switzerland, Ukraine; agreements have been initialised with Belarus, Belgium, Luxembourg, Netherlands, Croatia and Germany.

The strengthening of the eastern and south-eastern border of Latvia is continuing. In July 1998 an agreement was signed with the Siemens company on the technical securing of Latvia's eastern border in line with the requirements of the Schengen Agreement (see "Justice and Home Affairs").

## **Competition**

It became clear from the very start of transition that strong anti-trust legislation for free interplay of the market forces was needed. After realisation that supporting separate businesses by the public authorities could negatively influence competition, issues of the state aid control were also covered by competition policy.

In June 1997, Latvia adopted a new *Competition Law*. The Law is in conformity with the EU requirements on agreements, dominant positions and merger control. It applies to all sectors, including public enterprises. Enforcement of the new *Competition Law* is controlled by an independent Competition Council with its executive body - the Competition Bureau with thirty staff members. The decision-making body of the Competition Council consists of five members, approved by the Government for a five-year period. Thirty seven cases have been decided since establishment of the Council in January 1998 and sixteen cases are still under the investigation. In two cases, the decisions have been appealed in court.

The following regulations have been adopted: *On the Investigation Procedure of Violations of the Law on Competition*; *On the Procedure by which Agreements among Market Participants shall be Considered Valid*; and *On the Procedure of Submission and Examination of Reports on Merger of Market Participants*. These regulations contain the basic principles set out in the EC competition procedural legislation, including notifications, negotiation procedure, detailed rights and duties of the parties (the right to be heard, business secrets). Methodology on the form and content of notifications on the agreements among market participants was adopted by the Competition Council in May 1998.

A regulation *On Exclusive Distribution Agreements and Exclusive Purchasing Agreements Exempted from the Prohibition of the Restrictive Agreements Provided by the Competition Law* was adopted in March 1998. Several other regulations are under preparation (specialisation, franchising, research and development, transfer of technology agreements).

The *Competition Law* is to be supplemented by the draft law *On Regulation of Public Services* which will strengthen control over the energy supply monopoly utilities, reorganise tariff regulatory system, create a joint institution and promote enlightened market tariffs and improved payment discipline.

In order to establish a general framework for the state aid policies which complies with EU law, in February 1998 the law *On Control Over State Aid to Entrepreneurial Activity* was adopted. The Law ensures fulfilment of Latvia's international obligations, hinders misuse of public resources, and prevents competition distortions in domestic market.

Latvia has a fully functioning and consistent state aid control system. The independent State Aid Surveillance Commission consisting of 13 members was established and has extensive powers including access to information and rights to recover illegal aids. So far the Commission has adopted formal decisions on 2 state aid projects. The Commission had possibility to influence legislation in the sphere of regional aid, aid to SMEs and aid to development of mortgage crediting. Close attention is paid by the Commission to transparency as the decisions of the Commission are public. The Commission publishes surveys on state aids being granted in Latvia.

### **3.2 Innovation**

#### **Information Society**

Latvia is actively pursuing modernisation and establishment of the legal framework for information and communication technologies. In order to promote an information society in Latvia, a large scale National Programme "Informatics" has been prepared under the supervision of the Ministry of Transport. The Programme will provide general public access to information and data exchange between municipalities, towns and main registers. Currently, the Programme is being fine-tuned before being transmitted to the Government this autumn.

A law *On Personal Data Protection*, elaborated in order to ensure the rights of any person to protect her rights and freedoms processing the personal data manually or electronically, currently is under consideration in Saeima. The Law provides for establishment of an independent monitoring institution - the State Data Inspectorate.

The laws *On the State Information System (Register)* and *On Protection of Data bases* will be submitted to the Government before the end of this year. The draft law *On Publicity of State and Self Government's Information* is under consideration in the Saeima. Two programmes concerning information technologies have been launched - "Implementation of information technologies in education" (budget investments for 1998 - LVL 620,000) and "Informatisation of the education system" (budget allocation for 1998 - LVL 450,000). The laws foresee that by 2003 all general and professional educational facilities in Latvia will offer a computer class and provide a common network and access to the Internet.

## **Education, Training and Youth**

Latvia is actively pursuing reforms at all levels of education. In order to improve the cost-effectiveness and quality of the education system, preparations of a significant World Bank financed Education Reform Project are under way, and the loan agreement for USD 30 million is expected to be signed by the end of 1998.

At the beginning 1998, draft laws *On Education* (to replace the 1991 Law), *On General Education* and *On Vocational Education and Training* have been submitted to the Saeima. A law *On Youth* is being drafted and should be submitted to the Saeima by April 1999.

Furthermore, National Classification of Education (national version of ISCED 97) was introduced and the methodology of Development of National Qualification Structure System and National Occupational Standards was accepted by the National Conference on Higher Professional Education and Training Reform. Further developments in this field are envisaged by the PHARE '97 programme *Vocational Education and Training 2000* which starts in 1999. With the aim to promote the development and modernisation of vocational education and training, the Agency for Vocational Education Development Programmes was established in 1995. Currently, the Agency is responsible for 4 Phare programmes.

In order to assist with the reform of higher education, two non-governmental institutions (Higher Education Evaluation Centre and Academic Information Centre) are offering activities related to academic recognition of diplomas and periods of studies within the framework of ERASMUS. It is anticipated that by 2003, all Latvian higher education programmes will be compatible with those of EU Member States including implementation of sectoral Directives concerning mutual recognition of professional qualifications. In July 1998, Baltic States' Governments agreed on the creation of a common education space in general secondary and vocational education.

From 1998, Latvia is participating in the SOCRATES, LEONARDO DA VINCI and YOUTH FOR EUROPE programmes. Respective national agencies and a Co-ordination Council of EU Education Programmes have been established. Implementation of TEMPUS II *bis* programme began in 1998.

In 1998, there has been an increase of around 9% in educational expenditure from the state budget. Subsequently, an additional LVL 3.4 million have been allocated from 1998 budget accumulation to increase teachers' salaries.

## **Research and Technological Development (RTD)**

The Ministry of Education and Science has identified priority research directions: (1) information technology and telematics; (2) life sciences and biotechnology, pharmacy; (3) new materials and technologies; (4) ecology and environmental protection; (5) forestry and wood sciences. The mentioned areas are already competitive within the EU. Two universities and several scientific institutions participate in 25 research projects within the framework of EU RTD programmes.

Total expenditure on RTD is around 0.5% of GDP. In 1998, there has been an increase of 8% in state budget allocations for RTD. The PHARE programme *University and Science Reform* for 1998-1999 provides substantial assistance (150,000 ECU) in line with actual priorities.

The concept for creation of the National Innovation System, accepted on 24 March 1998, involves a number of innovative activities which are already in progress: (a) integration of national research potential within higher education, (b) creation of the state research centres to concentrate high quality research potential; (c) participation in the International Network of Innovation Relay Centres FEMIRC-LATVIA; (d) RTD co-operation with other countries and international organisations within the framework of EUREKA, COST and SOCRATES programmes. This Project will start in 1999.

Recently, the Concept of Development of Higher Education and Science has been submitted to the Government. Its main goals are to promote the role of science and higher education, the entry of new generation in these fields and to establish and strengthen the mechanism of 'return' of RTD.

Latvia expressed its intention to join the EU 5th Framework Programme for RTD.

## **Telecommunications**

In 1998 Latvia is continuing a comprehensive reform at the telecommunications sector, developing the new Telecommunications Sector Policy for the period 1998 to 2003. The policy calls for full liberalisation by 2003 and creation of a telecommunications regulatory environment in line with the *acquis*.

Latvia is among the leader countries in the Central and Eastern Europe for phone penetration (29.8 per 100 inhabitants) and share of phone digitised lines (25.5%). The draft of a new *Telecommunications Law* will be submitted to the Saeima before the end 1998. A draft Law provides for the establishment of a new regulatory

institution, an independent National Telecommunications Regulator. This will be the main driving force of further reform in the telecommunications sector. A Telecommunications Standardisation Technical Committee has been recently created to implement European telecommunications standards thereby achieving reliable interaction between networks.

Certification procedures for telecommunications and radio communications equipment were revised in August 1998 to comply with requirements of EU directives and to facilitate development of the market.

### **Audio-visual**

In negotiating its adherence to the WTO, Latvia followed the EU audio-visual policy. The law *On Radio and Television* is harmonised with the *Television Without Frontiers (TSF) Directive*, including European norms on the proportion of European works and of works produced in the Latvian language, on the proportion of independent producers, on the freedom of reception and jurisdiction, as well as on the advertising, sponsoring and protection of minors. The amendments are expected to be adopted by the Saeima before the end 1998.

The independent regulatory body is the National Radio and Television Council (NRTVC), with nine members appointed by the Saeima and nine executives. The main role of the Council is to issue broadcasting licences and monitor observance of the Law. Over the first seven months of this year, the NRTVC has made 23 rulings and prepared 5 administrative reports that were sent to the judicial authorities.

Latvia intends to join the Media II programme and in co-operation with other European countries to develop the intellectual and production output of the industry.

## **3.3 Economic and Fiscal Affairs**

### **Economic and Monetary Union**

Latvian authorities have a clear cut policy on the EMU: Latvia must be able to join the European Monetary Union at the time of its accession to the EU. The Government and Bank of Latvia have adopted macroeconomic policies designed to strengthen stability which are compatible with the principles of the EMU. Latvia already fulfils several convergence criteria of the EMU (public debt and budget deficit) and, in principle, complies with the exchange rate stability criterion. Attaining the required price stability and interest rate levels is among the targets of the Government's medium-term economic policies.

Amendments to the law *On the Bank of Latvia* will exclude the possibility of the government borrowing from the Bank of Latvia. In fact, such borrowing has not taken place for the last two years.

Statistics relevant to joining the EMU:

- 1) Latvia's fiscal surplus reached 1.3% of GDP in 1997. The Medium-term economic strategy aims at restricting possible fiscal deficit at 0.5% of GDP;
- 2) the public debt decreased from 14% of GDP in 1996 to 12% of GDP in 1997;
- 3) 12-month inflation decreased to 5.4% in May 1998;
- 4) annual interest rates for government securities - 1-month up to 1-year T-bills and 2-year bonds are fluctuating around 4-9%.

It is evident that a strong and stable financial sector is a critical pre-requisite for participation in the EMU. The sustainable development over the past years clearly indicates that Latvia should not encounter any problems in this area.

The stability of the national currency is proved by the fact that the peg of LVL to SDR has been maintained successfully for more than three and a half years.

### **Taxation**

From the very start of transition, Latvia has been paying close attention to reorientation of the tax system towards the principles of the market economy. At the moment, the Latvian tax system generally complies with the EU regulations. The transposition of the main requirements of the EU normative basis on taxation will have been completed by the end of this year. The Latvian tax system will have been brought into full accordance with EU standards by 2003.

During 1997 the Latvian Government continued approximation of legislation on the value-added tax with EU requirements, although the basic principles of the relevant EU directives had already been introduced in 1995. The latest changes to the VAT legislation, introduction of a special scheme for second hand goods, abolition of some discriminatory measures concerning the treatment of imported goods (these existed in respect to

newspapers and magazines), the introduction of a refund scheme for foreign tourists and the abolition of some limitations to the right of deduction of input tax became effective in January 1998.

In the medium term, the Latvian authorities will focus on the exemptions from VAT (i.e. gradual cancellation of the exemptions not provided for in the EU legislation). For the time being, the Latvian legislation does not provide for repayment of VAT for foreign legal entities. In the majority of countries this system functions according to the principle of reciprocity and is based on exchange of information. This system is expected to be introduced in Latvia by 2003.

In order to comply with EU legislation on the excise tax system, new excise tax laws concerning mineral oils, alcoholic beverages and tobacco articles have been drafted. These laws will introduce a warehouse system for excise-taxable goods, determine the suspended tax payment procedure, define the structure of taxable products and co-ordinate the list of exemptions.

A new law *On Excise Tax on Mineral Oils*, come into force on 1 January 1998 and provides that excise tax on mineral oils is imposed at progressive rates which are gradually increased every year. In 2001, the rates of excise tax on mineral oils will not be lower than those set by the EU.

It is planned that new laws *On Excise Tax on Tobacco Articles* and *On Excise Tax on Alcoholic Beverages* will be adopted during this year and come in force from 1 January 1999. The draft law *On Excise Tax on Tobacco Articles* will set an excise tax rate on cigarettes which is lower than that determined by the relevant EU directives. At present, excise tax on cigarettes is determined as a particular tax on one cigarette, constituting about 30% of the retail price. It is envisaged that excise tax rates on tobacco articles will be established in accordance with the minimum level set out by the EU by 2003.

The law *On Excise Tax on Alcoholic Beverages* is one more step towards approximation of the Latvian excise tax system with EU requirements. This law will come into force on 1 January 1999. Excise tax rates for alcoholic beverages already exceed the minimum level set out by the EU. For the time being, excise tax is levied only on beer with an alcohol percentage of 5.5 or higher. The possibility of taxing beer of lower alcohol percentage in line with EU requirements is being considered.

The State Revenue Service has established efficient cooperation and co-ordination through tax conventions with the tax administrations of Sweden, Finland, Denmark and the Netherlands. As of 1 January 1998, exchange of information is possible with fifteen states. Conventions with Germany, France and Italy have also been concluded (these will be ratified in the near future). Negotiations on conclusion of tax conventions are continuing with Belgium, Austria and Portugal, as well as with several non-EU states.

Latvia is a party to the European Organisation of Tax Administrations (IOTA) and is represented in this organisation by the State Revenue Service.

## **Statistics**

The law *On State Statistics* was adopted by the Saeima in November 1997. The Law fully complies with the regulation *On Community Statistics*. The fundamental principles of Latvian statistics are impartiality, reliability, relevance, effectiveness, confidentiality and transparency.

The following progress towards the compatibility with EU standards, fulfilling the tasks of the Accession Partnership and the National Programme for Adoption of the *acquis* has been achieved:

- the cooperation of the business register with administrative registers has been intensified in order to supplement the business register data base with information on localised activities;
- in order to develop business statistics, national and agricultural accounts, Latvia has followed the Eurostat's Statistical Requirements Compendium in implementing a succession of new statistical surveys financed by the national PHARE programme (a production cost survey, a survey of main raw material consumption in industry, a survey on transport of goods by road and others). The main components of the shadow economy, the import price index as well as input-output tables have been calculated. A new register of rural farms has been set up and is expected to be fully operational by 2000;
- preparatory work for the Population Census 2000 and Agricultural Census 2000 has begun;
- the concept of an integrated data processing system has been worked out and its implementation has begun;
- significant work has been done in order to implement the EU classifications (PRODCOM, CPA, CC) so that by the end of 1998 all the main statistical classifications adopted by the EU will have been adopted by Latvia;

The full completion of work to upgrade the statistical system is scheduled for 2003. Special attention in the statistical upgrading programme is devoted to the improvement of legislation according to EU requirements.

Improvement of the statistical system is included as a priority in the National Program for Adoption of the *acquis*.

### 3.4 Sectoral Policies

#### Industry

In 1997, GDP growth was boosted by a strong resurgence of industrial production. The food processing, wood-processing and textile industries led the way. Industrial output increased by 11.8% in 1997 as compared to 1996. In the first quarter of 1998, the growth rate of manufacturing was 13.6% in comparison to the same period in 1997. The proportion of employees in industry increased from 20.8% in 1996 to 21.3% in 1997. The share of the industrial sector in GDP was 18.2% in 1996 and 18.4% in 1997.

The privatisation of state-owned industrial enterprises is almost completed. 90% of the manufacturing sector has been privatised.

The PHARE enterprise-restructuring programme was prepared in 1998 and will be financed by the Catch-Up Facility funds in 1999. The programme plans to support the restructuring of 15-20 medium and large enterprises, and to support the development of the textile, machinery and bioenergy sectors.

Accumulated foreign investments at the end of 1997 were LVL 138.8 million or 26.1% of all foreign investments in Latvia (compared to 17.1% in 1996). In 1997, almost half of all foreign investments were made in manufacturing companies.

Exports of industrial products increased by 22.2% in 1997. Export to the EU countries increased by 33.6%, reaching 48.9% of the total industrial export volume. The main export goods were wood products (30%), textiles and related goods (16%), agricultural and food products (15%). The metal and machinery manufacturing industry accounted for 20% of exports.

In order to promote the competitiveness of their products in the European market, ten Latvian companies in different sectors have applied for and received ISO 9000 quality assurance certificates. Interest in quality assurance as set by ISO 9000 is rapidly growing. It is expected that over the next few years the number of companies certified by ISO 9000 requirements will increase substantially.

Food and beverage production employs 26% of all labour employed in manufacturing and accounts for 43% of the total manufacturing production output. The growth rate of output in 1997 was 7% as compared to 1996.

Production of wood and wood products is the most dynamic sector, mainly oriented towards export to the Western market. This sector employs 11% of all labour employed in manufacturing, producing 12% of the total manufacturing production. Growth rate of output in 1997 was 9.1% compared to 1996.

Textile manufacture accounts for 12.3% of the total added value of manufacturing. In 1997 textiles production has increased by 5.6 % and employment increased by 1.7% in the textiles industry. This sector employs 9% of all labour in manufacturing while producing 7% of the total manufacturing production. Exports of textile goods to the EU countries have been increasing annually and reached 59.2% of total exports of textiles in 1997; this is an increase of 25% compared to 1996.

#### Agriculture

At the present stage of development, the main target of agricultural policy is to convert agriculture into a sector which is able to integrate into the common European market. Latvia has a set of government policy documents, *The Concept of Agricultural Development*, which include long term principles of state support, and the *1997 Agricultural Report. Sectoral Development Policies* and the *Annual Agricultural Development Programme* will be finalised in autumn 1998. Latvia is implementing a rural diversification programme which provides financial support to investment in rural areas. Latvia has begun to establish the administrative structures required for the Special Action for Pre-accession for Agriculture and Rural Development.

Land reform in rural areas is now completed. 90% of agricultural land is in private use. 47% of agricultural land is used by large-scale private farms. The average size of family farms has increased each year and is now 24 hectares.

Latvian policy on forestry co-ordinates the implementation of social, economical and ecological functions of forestry in the framework of the Helsinki and Lisbon resolutions, as well as the European forestry protection process. In the first phase of optimisation of forestry management, the legislative and policy functions have been separated.

Since 1996 GDP in agriculture, hunting and forestry has grown by 4.9% (GDP growth per employee rose by 6.7% in the same period). Agriculture now represents 8.1% of Latvian GDP. Privatisation is almost complete in the food marketing and processing industry, which represented 8.4% of Latvian GDP in 1997.

In 1997, the share of agricultural trade was 14.51% in imports and 14.53% in exports. Timber forms 30% of Latvia's export volume. The main exports are dairy products, fish and processed agricultural products. In 1997, the Association Agreement Protocol No 2 was revised, thus further liberalising trade in processed products. Six Latvian dairies, five fish processing enterprises and four fish refrigerator ships are allowed to export their production to EU countries. Liberalisation of foreign trade in the 1997 took place in line with WTO conditions.

Agricultural subsidies formed 2% of the state budget in 1997 and 3% in 1998, in accordance with the law *On Agriculture*. Support is mainly directed to increasing the competitiveness of Latvian agricultural products for example by technological modernisation, food quality aspects, land reclamation, pedigree, seed breeding, non-traditional farming, rural development, education, science and credit guarantee fund.

In 1997, Latvia was self sufficient with cereals, potatoes, vegetables, sugar and milk. In 1998, it is expected that the total yield of cereals will rise by 7% and sugar beets by 13%. In the first half of 1998, total milk purchases grew by 35% and meat purchases by 9% in comparison to the same period the previous year.

Latvia is carrying out national law approximation with EU laws, as well as restructuring and modernisation of inspection and control measures to meet the requirements of basic laws (see annex).

Agricultural and food product quality control is managed in two ways: (1) harmonisation of normative acts and documents in accordance with EU requirements; (2) defining of competence for food quality control (Decision of the Government, based on updated law *On Foodstuffs*). This creates preconditions for free movement of goods and consumer rights protection, corresponding to the Third National Programme for Integration into the EU.

Legal acts on proper production and distribution practice have been prepared for effective state control and supervision of animal food, veterinary medicine and veterinary pharmaceuticals in enterprises, warehouses and markets.

The regulation *On Intervention in the Cereals and Milk Market Sector* have been approved by the Government and transferred into intervention provisions and principles for the milk and cereals market in conformity with the CAP.

The law *On Breeding* and regulation *On Animal Identification* were adopted in 1998, clearing the way for implementation of an animal identification and registration system in accordance with EU requirements. A cattle identification system is already in place.

Latvia intends to optimise the functions and structures of veterinary and plant protection supervisory bodies, to introduce measures for animal welfare and protection, as well as set up a unit for harmonisation of national veterinary legislation with EU requirements. A plant quarantine organisms surveillance programme has been initiated in Latvia. The system for plant protection aid registration, usage and control complies with EU requirements. Laws *On Veterinary Medicine* and *On Plant Protection* have been submitted to the Government.

Latvia still maintains the status of favourable territory in the area of infectious diseases of animals. A state programme exists for dealing with outbreaks of foot-and-mouth disease and classical swine fever. Veterinary regulation on import of animals and products of animal origin have been prepared. Export-import models of certificates are being harmonised with importing states.

The State Veterinary Service, State Food Quality Inspection and State Grain Inspection dealing with food supervision and control have been established under the auspices of the Ministry of Agriculture. The Department for Control of Products of Animal Origin operates under the auspices of the State Veterinary Service. 120 food quality inspectors have been trained. Latvia is establishing a network of modern animal disease diagnostic and production quality conformity laboratories. Five veterinary laboratories have been accredited as complying with Latvian National Standards and European Norms. A modern serological diagnostic of 17 different infectious diseases has been introduced. A residue control programme for food and animal origin products was introduced in 1998.

In 1997, a Sanitary Border Inspection Service (240 employees) under the supervision of the Ministry of Agriculture was established. There are 31 control stations and 62 customs warehouses. Ten prospective external EU border control points have been identified by the Sanitary Border Inspection.

The Ministry of Agriculture is responsible for Economic Agricultural Accounts. The Farm Register, Farm Accountancy Data Network and Integrated Administrative and Control System have been established in accordance with EU requirements. A market information system began to operate just recently.

Since 1993, PHARE projects amounting to 20 million ECU have supported the strengthening of the Ministry of Agriculture, modernisation/restructuring of the agricultural sector, creation of an extension service, land reform, law approximation, food quality, and rural diversification, among other things. This has resulted in improved Ministry of Agriculture management and co-ordination, a professionally accredited extension advice, creation of a land market, raising of the food quality level based on HACCP, improved border control, better control over animal registration, and improved veterinary and phytosanitary services and laboratories.

## **Fisheries**

To ensure development of the fisheries sector and structural policy, the programmes "Baltic Sea and Coastal Fleet Development Program" and "Fish Industry Development Program" were created within the framework of the National Fisheries development program. These programs were adopted by the Government in July 1998 and include completion and harmonisation of national legislation, development and maintaining of international contacts in fisheries and modernisation of structures in fisheries and fish processing, in accordance with EU and international requirements (see annex).

In 1997, fishery accounts for 0.24% of GDP and 14,000 people were employed in the fisheries sector. The total catch in 1997 was 105,391 tons. Total import of fish and fish products amounted to 58 000 tons, with exports of 125,000 tons. The foreign trade balance was positive at 19.6 MECU.

The regulation on *Commercial Fishing Regulations in the Territorial Waters, Economic Zone Waters* and the regulation *On Hygiene Requirements for the Production and Placing on the Market of Fishery Products* (in force since March 1998) are fully in accordance with the requirements of EU. The draft Regulation *On the Catch Landing Declaration Control System in the Ports of the Republic of Latvia* will meet the requirements of EU. After approval of these regulations, the number of inspectors will increase to 35, and the fishing and landing control technical base (land and marine transport, communication system) will be modernised.

In the medium term, the fishery sector does not appear to pose any major difficulties to the pre-accession process, but the fishery administration structure in Latvia needs to be enlarged in order to ensure practical implementation of legislative measures, especially in control of fisheries policy and fish production quality.

## **Energy**

According to the *Avis*, Latvia's energy policy is in line with EU principles. The integration of the Latvian energy sector into the EU internal market is based on the Latvian National Energy Development Program, the Concept on National and Municipal Heating, the Treaty for the European Energy Charter (submitted to the Saeima) and the law *On Energy* adopted in the second reading by the Saeima in July 1998. The law *On Energy* covers competition increase, energy prices, access to energy transmission networks, preparedness for emergency situations (including reserves of oil products), effective use of energy, and implementation of environmental protection legislative acts.

The National Program of Power Sector of Latvia was approved in September 1997. Its objective is to establish a set of activities aimed at stable provision of energy resources, quantities and quality corresponding to demand of customers, at possibly lower cost and less impact on the environment. The program is developed for the time period until the year 2020. It is a planning document which unites in common system the interlinked technical, economic, and organisational activities and consist of 12 sub-programs.

Privatisation of Joint Stock Company *Latvijas Gaze* and State Joint Stock Company *Latvenergo* continues. To develop competition and the energy market, the following documents have been approved: the regulation *On Gas Supply and Usage*; the *Concept on Amendments in Tax Laws due to Oil Trial and Exploration Works*; and the draft regulation on *Oil and Natural Gas Trial and Exploration*.

The aim of the draft law *On Regulation of Public Services* (currently under consideration in the Saeima) is to strengthen control over the energy supply monopoly utilities, reorganise the tariff regulatory system, create a unified institution and facilitate enlightened market tariffs and improved discipline of payments.

The regulation of the Government *On Prevention, Restriction and Control of Emission of Atmosphere Pollutants from Burning Installations in Energy Production and Industry* have been prepared and will be adopted by the end of 1998.

The Energy Supply Regulatory Board has developed and approved new calculation methods for energy supply tariffs for heat and gas (a draft for electricity also exists). These provide economical costs for development of energy supply utilities. The Energy Supply Regulatory Board has distributed licences for all electricity and gas supply utilities. Licensing of heat supply utilities will soon be completed.

Legislative acts related to oil and oil product transit through pipelines are being gradually amended to comply with EU directives. Existing legislative acts basically ensure environmental protection, security,

competitiveness and needs related to transit. The aquatory of the Ventspils port has been deepened by 17.5 metres. The reconstruction of a reservoir park at the Ventspils terminal is continuing. Measures are being taken to incorporate existing the pipeline infrastructure into the Trans-European Network (TEN).

The Joint Stock Company *Latvijas Gaze* has ensured the installation of gas meters for all supply systems and consumers. Installation of gas meters in apartments will soon be completed. Both heat supply utilities and consumers continue to install heat energy meters, regulatory facilities and water meters in flats.

The only small nuclear research reactor in Latvia (at *Salaspils*) was closed down in June 1998 and will be dismantled.

Modern gas, oil and oil product metering stations for transit pipelines on Latvian borders have been built. Latvia could provide useful underground gas storage capacity of strategic benefit to the EU.

Co-operation is continuing among Baltic Countries and Baltic Sea Countries in the electricity transit project "Baltic Ring" and in assessment of plans for uniting gas pipelines.

Financing has been assigned to energy supply projects in the framework of the Public Investment Programme. According to the Government Policy for the Energy Sector, priority is given to projects related to usage of domestic energy resources (wood, peat) and enlargement of energy efficiency, including cogeneration. The Latvian Development Agency has also attracted investments and they are working on establishment of the Energy Efficiency Foundation.

Under the financing memorandum for the PHARE programme-1997 signed between the European Commission and Latvia a deposit of 2.6 MECU has been allocated for a revolving fund for investments in projects within energy efficiency. Also a deposit of 1 MECU is expected to be available from the PHARE 1995 budget.

## **Transport**

The favourable geographical position of Latvia, its location along the Baltic Sea rim, and non-freezing ports provide excellent opportunities for the development of passenger and cargo transportation.

The National Program for Transport Development was approved in 1995. In February 1998, the Co-ordination Council for this program approved the Programme for 1998-2000. It contains actualisation, a detailed description, and specification of activities for the period of three years. Implementation of program in 1997 helped to maintain and develop transport infrastructure meeting certain quality criteria, to perfect the system of transport services, to improve traffic and to maintain a progressively higher safety of traffic.

The share of the value added by the transport sector in GDP in 1997 was 17.2%, an increase of 7.4% from 1996. The transport sector employs 8.5% of all those employed in national economy.

Further adaptation of national laws and regulations in the field of air transport has taken place to meet EU requirements. A number of technical and operational regulations have been developed on a Joint Aviation Regulations basis. In July 1998, Latvia was accepted as a candidate member state by the Joint Aviation Authorities Board. National regulations introducing a code of conduct for computerised reservation systems were drafted.

Latvia is working on a State Port Control and Action Plan for implementation of the requirements of the Paris Memorandum of Understanding and Directive 95/21. The Action Plan will include a training program of State Port Control inspectors. In order to comply fully with international standards, the Tonnage Convention was ratified and the 1998 SOLAS Protocol has been translated into Latvian and is being prepared for ratification.

Latvia has joined the basic maritime conventions regarding maritime safety and pollution prevention. Latvia has prepared a National Oil Spill Contingency Plan. A number of projects have been initiated - a vessel traffic system, installation of a satellite navigation system based on the Differential Global Position System, establishment of a search and rescue communications system, and modernisation of equipment for oil spill cleaning operations. Latvia has ratified the most important international conventions relating to marine environment protection: MARPOL 73/78, Protocol to CLC 92, and Protocol to FUND 92.

Privatisation of the largest Latvian shipping company, the state joint stock company *Latvijas Kugnieciba* began this year.

In April 1998, the Saeima adopted a Law *On Railways* which includes requirements of the following directives – the Development of Community Railways, the Allocation of Railways Infrastructure Capacity and the Charging of Infrastructure Fees, Licensing of Railway Undertakings. In accordance with the Law, the Railways Administration will be created by January 1999 and the Railways Technical Inspectorate by July 1999.

90% of the 169 directives on road transport will be implemented by the end of 1998, among them directives concerning type-approval systems, masses and dimensions, and admission to occupation, while requirements concerning speed limiters will be implemented by the end of 1999. Directives concerning driver's licences, training of drivers, tread depth of tyres, annual technical inspections, and safety belts have already been implemented. The highest degree of compliance with provisions of Regulations is in the field covered by the AETR Agreement and governed by Regulation 881/92 (access to the market).

Several PHARE co-financed projects were implemented in 1998 in transport sector.

### **Small and Medium Enterprises**

Small and medium enterprises (SMEs) play a very significant role in the Latvian economy. Currently, SMEs account for 96% of all enterprises registered in Latvia. About 70% of the Latvian population is employed in SMEs. The SMEs are dominant in the major export industries, such as wood processing, foodstuffs and textiles.

In order to promote a favourable environment for the development of SMEs, to strengthen their competitiveness, as well as facilitating their entering into the international market, the Government has adopted the National Programme for Small and Medium Sized Enterprise Development. The Programme provides aid and assistance for entrepreneurship, training, consultations and financial resource availability. A network of nine Business Advisory Service Centres (BASC) has been established. In addition, Business Innovation Centres (BIC) have been established to support technology-oriented SMEs and promote the transfer of new technologies. The network of BASCs has been extended with assistance from the PHARE SME support programme. Training programmes at three levels have been offered to more than 150 companies within the framework of the PHARE SME programme.

The Latvian Guarantee Agency was established in January 1998. Plans are underway to enlarge the Latvian Guarantee Agency reserve capital from 1.4 MECU to approximately 2.5 MECU in 1999 and to create an SME Innovation Fund (envisaged capital is approximately one MECU) in co-operation with other financial institutions.

## **3.5 Economic and Social Cohesion**

### **Employment and Social Affairs**

The main directions of labour market policy are (1) to promote professional training and retraining of the unemployed; (2) to establish special labour market programmes for long-term unemployed and disabled persons; (3) to organise paid public works targeted at the long-term unemployed; (4) to open additional employment offices; (5) to provide additional financial funds for regions with a high unemployment rate. Information technology has been developed to establish an information network for all 27 regional branches of the National State Employment Service. In 1997, 49.9% from all unemployed who have had professional training and retraining started to work.

The official unemployment rate at the end of 1997 was 6.7% (14.4% according to ILO methodology). The number of unemployed levelled out over the past year and in 1997 and in the first half of 1998 the number of newly registered unemployed has decreased as a result of increasing economic growth.

Amendments to the Labour Code have been prepared so that they correspond to the requirements of the EU *acquis*. The new draft of the Labour Code will be submitted to the Government in October 1998.

A new version of the law *On Labour Protection* has been drafted in order to implement the relevant *acquis*. Regulations on the protection of workers from risks related to exposure to asbestos and biological agents at work, and the provision of safety and health signs at work have been submitted to the Government. In October 1997, the Government accepted the White Paper *On Establishment of a Guarantee Institution to Address Employee Petitions in Cases of Employer Insolvency*. Before the end of 1998, a draft law *On the Guarantee Institution* will be submitted to the Government.

Latvia is moving ahead successfully with social reforms. Large scale reform of the pension system consisting of three tiers will be progressively implemented in order to become fully effective by 2002. The first tier of the pension system - a state mandatory non-funded pension scheme (NDC PAYG) - has been implemented since 1996; the law *On the Mandatory Funded Pension Scheme* has been submitted to the Government; a voluntary private funded pension scheme as a third tier began operating on 1 July 1998. The minimum pension age is gradually being raised, reaching 60 years for both men and women after 1 July 2004.

The new legislation on maternity, sickness and unemployment insurance, as well a new kind of mandatory social insurance against work accidents and professional diseases came into effect at the beginning of 1997.

Since January 1, 1998, the State Revenue Service is responsible for collecting social insurance contributions, thereby making tax administration more effective. A social insurance administration - the State Social Insurance Agency, is being developed in order to implement necessary social security co-ordination legislation in the perspective of the full EU membership.

In order to assist families, the child care benefit was recently increased by 240% for families with a child under 18 months. In 1997 social assistance, insurance and health care reached 19.1% of GDP.

Improvements to the health care system are continuing. The principle of equal opportunities in the access to the necessary health care services is being respected. Rationalisation of the health care financing system has been carried out. In place of 33 Medical Insurance funds, 6 new Medical Insurance Funds and 2 Account Funds were established with the help of municipalities, thus increasing the cost efficiency of health care services and increasing accessibility to services. In March 1998, the law *On Health Care* was amended to promote the quality of health care services by providing for certification health care institutions, their structural units and quality assessment of medical equipment.

Present legislation prohibits direct or indirect discrimination on the grounds of gender.

Directives *On Tar Content in Cigarettes* and *On Labelling of Tobacco Products* have partly been implemented in the Law *On Restriction of Manufacturing, Sale Advertising and Smoking of Tobacco Products*. It is expected that the Directive on tar content will be fully implemented by 2002 and the Directive on labelling of tobacco products - by 2000.

PHARE was one of the main financial supporters providing assistance to health finance restructuring, the social insurance sector, the pharmaceutical sector policy and to institutional development for a more effective labour market.

### **Regional Policy and Cohesion**

In 1997 and the first half of 1998, the division of competencies between the institutions and administrative structures responsible for integrated regional development program management was considerably improved.

The laws *On Territorial Development Planning* (with the aim to promote implementation of a policy for sustainable development) and *On Administrative and Territorial Reform* (with the aim to form capable and efficient local authorities) are under consideration in the Saeima.

In January 1998, the Government adopted *The Concept of a National Spatial Plan* with the aim to facilitate formation of co-ordinated regional policy, to ensure protection of the environment, rational use of territory and natural resources, to manage and protect nature and cultural and historic heritage and to establish preconditions for a connected network of settlements and infrastructure.

In May 1998, the law *On Assisted Regions* was adopted with the aim of accelerating development of regions of special concern. The Government has adopted the package of six regulatory documents linked with this law, which are mainly related to the Regional Fund. The task of the Regional Fund, established in April 1998, is promotion of entrepreneurial activity in the assisted regions.

The Regional Development Council was established in 1997 for the co-ordination of regional development matters at central government level and for co-ordination of central, regional and local government activities.

A Special Preparatory program for Structural Funds was initiated by the European Commission. Within the framework of this comprehensive program several specific pilot projects will be developed.

Following projects on Regional Development are elaborated:

- the Program for Rural Development in Latvia (this program was approved by the Saeima in June 1998; the aim is to define the goals of rural development policy and to determine the steps and actions necessary for achieving these goals).
- the Integrated Coastal Zone Management Project (an integrated approach involving state and local government institutions, and both the public and private sectors).
- the Pilot Regional Development Plan for the *Latgale* Region (designed to enhance capacity for regional development activities and creating effective access to the assistance programmes).

A state subsidy for physical planning and development planning has been allocated to local municipalities annually since 1996 for preparation of development and land use plans. In order to receive the grant, municipalities are obliged to participate with their own financing.

Following the decision of the European Integration Council an Inter-Ministerial Structural Funds Working Group has been established. The Structural Funds Co-ordination Division was established at the Ministry of Finance, which will be responsible for the Special Preparatory Programme for the Structural Funds in Latvia. The purpose of the Programme is to prepare the Latvian administration for Structural Funds planning, implementation, financial control and monitoring.

### 3.6 Quality of Life and Environment

#### Environment

Strategies for the main environmental areas have been elaborated and overall co-ordination takes place in the EU-integration unit at the Ministry of Environmental Protection and Regional Development.

In order to solve water supply and waste water treatment problems in Latvia, work has been divided into two phases - (1) Implementation of *Programme 800+* and subsequently (2) achieving full compliance with the EU Directives in water and waste sectors.

The Strategy for the Development of Water Supply and Waste Water Treatment in Small and Medium Sized Towns of Latvia was approved by the Government in January 1997 and *National Programme 800+* (Water Supply and Waste Water Treatment in Small and Medium Sized Towns of Latvia) has been set up.

In Latvia there are 69 populated areas with more than 2000 inhabitants, altogether accounting for about 70 % of the population. Plans are underway to upgrade, refurbish or construct waste water treatment systems in all towns with more than 2000 inhabitants before the end of the year 2010.

Projects to improve water supply and waste water treatment in the three largest cities (which comprise 42% of the total Latvian population, or 60% of all urban dwellers) are on-going and are scheduled for completion in the year 2005. Currently projects are underway or complete in 58 towns. Ninety percent of the population in towns with over 2000 inhabitants (63% of the total population) will be served by the year 2005. The remaining ten percent will be served by the year 2010.

Hazardous waste management, collection and disposal of discarded pesticides is considered a very high priority. Pesticides will be collected and stored in a safe and environmentally reliable way in interim storage facilities at three sites for further treatment. The following projects are underway:

- Design of a new hazardous waste landfill;
- A tender for a mobile incinerator;
- The establishment of the hazardous waste institutions and management systems on a country-wide scale (expected to be in a place by September 1999).

The National Municipal Solid Waste Management Strategy was elaborated in 1997. The Strategy sets the direction for municipal solid waste management development in Latvia. Currently there are 550 operational and 160 closed-down dumping sites in Latvia. The establishment of a modern solid waste management system is being prepared in seven regions; the system will serve approximately 66% of the total population.

The main tasks for the implementation of corresponding EU directives in the solid waste sector are the following:

- to establish ca. 10-15 regional sanitary landfills,
- to reorganise the waste collection and transportation system,
- to investigate and make an inventory of existing dumping sites,
- to take remedial actions for existing landfills.

The Nuclear Research Reactor at Salaspils was closed down in June 1998. The Concept for Decommissioning is being prepared. Modernisation of the institutional framework, upgrading of the radioactive waste management infrastructure and development of an early warning system are considered main priorities; steps have been made this year to fulfil these priorities.

The National Programme of Adoption of *acquis* contains an important section on the environment. A Concept for Development of the *Environmental Protection Law* has been drafted. The Latvian Approximation Strategy and Action Program was prepared in July 1998. Preparation of sectoral implementation strategies began in August 1998.

There has been noticeable improvement in almost all environmental sectors, especially in air quality, and in water contamination, waste management and reduction of industrial pollution:

- **Air** the regulations *On the Ozone Layer Protection* and *Fuel Quality* were adopted. Several new draft regulations on air quality standards, large combustion plants, and VOC emissions have been prepared and will be adopted this year.
- **Waste** the law *On Municipal Waste* is nearing adoption by the Saeima. The majority of EU Waste legislation will be transposed in 1998.
- **Water** EU water quality standards for drinking, bathing and surface water were partly transposed in 1997 and will be fully transposed in 1998. Latvia's approach to the Water Framework directive is being developed.
- **Nature Protection** Legislation is well-developed, but efforts must still be made to ensure compliance with the regulations. Full legal compliance in this sector is expected by the year 2000.

- **Chemicals and GMOs** A new Law *On Chemical Substances and Chemical Products* was adopted in April 1998, and 8 Cabinet Regulations are now in preparation. Legislation on GMOs is expected in 1999.
- **Industrial Pollution** a Concept on IPPC Legislation has been developed. The Law *On Pollution* and regulations on IPPC are expected to be passed in 1999. Regulations on the Seveso directive will be adopted by the end of 1998.
- **Nuclear Safety** five new legal acts had been adopted since the Commission's *Avis* and four more are expected this year.
- **Horizontal Legislation** EIA Regulations are close to adoption by the Government.

To strengthen and co-ordinate the approximation process, the European Integration Unit (3 employees) was created in the Ministry in August 1997 and the Department of Environmental Protection was strengthened with ten additional staff members working mainly on approximation issues. An "EU Steering Group" on EU integration issues was established at the end of 1997 and is co-ordinating general EU integration issues.

EU Integration Working Groups representing all involved ministries, as well as other institutions, have been established for all main sectors of legislation (Water, Waste, Air Protection, Chemicals, Nature protection, Industrial Pollution, and Nuclear Safety).

A non-profit "Environmental Project Agency" was established in 1997 to manage the increasing number of investment projects and to ensure implementation of the most costly directives in the water and waste water sector, while the Latvian Environmental Investment Fund has been set up to provide revolving funds for the public and private sector.

### **Consumer Protection**

A new draft law *On Consumer Rights Protection* will be discussed in the Saeima in the nearest future. The new draft Law is harmonised with several EU directives concerning unfair contract terms, doorstep selling, timesharing, distance selling and consumer credit. The law *On Advertising*, which incorporates directives concerning misleading and comparative advertising, will be drafted by January 1999.

The Consumer Rights Protection Centre (28 employees), established in May 1998, is the main institution responsible for supervision of observance of consumer rights protection legislation. The State Sanitary Inspection (180 employees), established in October 1997, is responsible for consumer rights protection in the area of circulation and distribution of foodstuffs.

The following regulations, in harmony with the *acquis*, have been accepted into law:

- *On the Safety of Cleaning Agents and Detergents* (in force);
- *On the Safety of Cosmetics* (in force from September 1998);
- *On the Labelling of Textiles* (in force from 1 January 1999);
- *On the Labelling of Foodstuffs* (in force from 1 July 1998).

Regulations on safety of the toys will be drafted by September 1998.

The PHARE Consumer Institution and Consumer Policy Programme project for establishing a Consumer Information Centre is proceeding.

The Council directive on package travel, package holidays and package tours will be controlled in accordance with regulations introduced this year.

### **3.7 Justice and Home Affairs**

In May 1997, Latvia elaborated *Latvia's Strategy in III Pillar issues*. The main directions of activity are: strengthening of the eastern border, gradual harmonisation of the policy on migration and refugees in accordance with EU standards, combating of organised crime with particular attention to prevention of drug trafficking and money laundering; the fight against corruption; improvement of the work of police and customs; and the improvement of the prison system.

In 1997, the government created an Inter-ministerial Working Group for co-ordination of III pillar issues. A special *ad hoc* group in the field of the III pillar has been established in the framework of the Baltic Council of Ministers. Latvia is also actively taking part in the Task-Force on Organized Crime in the Council of Baltic Sea States.

Latvia in cooperation with other Baltic states is elaborating the project of Baltic Government Data Communication Network in order to create a joint information infrastructure including authorities of customs, border control, immigration control and organized crime prevention with a view to join the European Business Register.

Border agreements have been concluded with Estonia, Lithuania and Belarus. Demarcation of the Latvian - Lithuanian and the Latvian - Estonian border will be finished in 1998, and demarcation of the Latvian - Belarussian border has already begun.

The draft agreement on state border has been accepted by the Latvian Government on December 9, 1997, thereby Latvian side have accomplished all internal procedures to prepare mentioned agreement for signing. Latvia will sign the agreement as soon as Russia is prepared to do so.

In order to raise efficiency of the State's Eastern Border control system, the National Border Construction Company (NBCC) "*Valsts Robezbuve*" was established in December 1997. Following the international tender for appropriate suppliers for the formation of the eastern border's technical protection and control and information systems, NBCC and Siemens Nixdorf signed an agreement on 31 July 1998. Siemens was selected along with the company Thomson CFS as a supplier of a border technical surveillance system which will be compatible with equipment used in Schengen countries.

The Government decided to establish a joint software network, information base and communication system for the state border institutions before 2001.

According to the amendments in the law *On the State Border* made in December, 1996, the State Border Guard was subordinated to the Ministry of Interior. After the adoption of the law *On the Border Guard*, since January 1, 1998, the Border Guard is under the supervision of the Ministry of Interior. The raising of professionalism within the Border Guard, which is carried out at the Border Guard College of the Police Academy and the Border Guard School in Rezekne is crucial for the eventual success of the project.

On 28 May 1998, Latvia together with other candidate countries acceded to the Pre-accession Pact on organised crime.

In January 1998, the Crime Prevention Program was adopted. In June 1998, the Interpol National Central Bureau of the Republic of Latvia was linked up to the Central Car Theft Automated Database of the Interpol General Secretariat. In February 1998, the Government adopted a *Concept on Prevention of Corruption*. The Anti-Corruption Council has been established.

The State Police are taking steps to improve the operation of individual units responsible for the fight against organised crime. In March 1998, the Bureau for Fighting against Organized Crime and Corruption was reorganised and its new by-laws adopted (125 employees). After the reorganisation of the Bureau, the effectiveness of its work and the number of the solved crimes have increased by 40%. In March 1998, a Smuggling Combat Co-ordination Centre was established under the supervision of the Finance and Interior Ministries and the General Prosecutor's Office.

Recently a unit responsible for witness security was established within the State Police, and at present intensive training for its 13 staff members is taking place.

A law *On the Prevention of Laundering of the Proceeds from Crime* came into force on 1 June, 1998. This Law regulates the rights and obligations of financing, credit and control institutions. The Convention on Laundering, Search and Confiscation of Proceeds from Crime of 1990 was signed in March 1998 and currently is under consideration in the Saeima. The Control Service started its operation summarising and analysing reports of financial and credit institutions on suspicious transactions. On 2 April 1998, the Latvian Criminal Code was supplemented by an article providing criminal liability for laundering the proceeds of criminal activities. The Government adopted regulation on ratification of the Convention of the Council of Europe *On Laundering, Search, Seizure and Confiscation of the Proceeds from Crime*.

Latvia has subscribed to the most important UN conventions (1961, 1971, 1988) in the field of combat against drugs and has aligned legislation accordingly. In May 1996, a law *On Precursors* was adopted.

A National Programme for the Combat of Drugs 1997-1998 has been adopted and implemented. Latvia's drug control and drug abuse prevention masterplan for the period 1999-2003 is currently under design.

The following institutions conduct operations in Latvia: the Interministerial Coordination Commission for Drug Control and for Combating Drug Abuse and the Drug Enforcement Bureau (31 employees) under the State Police. The Drug Enforcement Bureau primarily prevents the proliferation of drugs in Latvia and controls the transit of drugs and psychotropic substances.

On 1 January, 1998 the law *On Asylum Seekers and Refugees* in the Republic of Latvia, entered into force. The 1951 Geneva Convention relating to the Status of Refugees and the Protocol of 1967 was ratified in June 1997, but without geographical restrictions in October 1997.

Experts from EU Member States who visited the Olaine Centre for Illegal Immigrants in May 1998 acknowledged that conditions at the Centre meet EU requirements. Construction work is continuing on a resettlement centre for asylum seekers at Mucenieki.

The law *On Asylum Seekers and Refugees* states that examination of applications for refugee status, control of information provided by asylum seekers, decision-making on granting refugee status and issuing of refugee identification and travel documents is mandated by the Centre of Refugee Affairs, a structural unit of the Citizenship and Migration Affairs Agency of the Ministry of Interior.

At present the applications of 13 asylum seekers have been examined. Following a negative result, two of applicants have lodged their case at the Appeal Council of Refugee Affairs where an outcome is pending.

Since January 1997, bilateral visa-free regimes have entered into force between Latvia and Andorra, Denmark, Ireland, Liechtenstein, Malta, Norway, Finland, Switzerland and Sweden. Agreement on visa regime abolition have been signed with Slovenia.

Latvia has concluded agreements on the readmission of persons residing illegally since July 1997 with following countries: France, Italy, Liechtenstein, Norway, Switzerland, Ukraine, have been initialised agreements with Belarus, Belgium, Luxembourg, Netherlands, Croatia and Germany. Latvia will sign the readmission agreement with Russia as soon as Russia is prepared to do so.

The co-operation between courts of Latvia and other countries is based on the Convention on the Transfer of Sentenced Persons (1983); the European Convention on Extradition (1957); the European Convention on Mutual Assistance in Criminal Matters (1959); and the European Convention on the Transfer of Proceedings in Criminal Matters (1972). Court reform is continuing. At present, plans are underway to enlarge the Court Department of the Ministry of Justice in 1999.

Co-operation in the legal field with such countries as Estonia, Lithuania, Russia, Belarus, Poland, Ukraine, Moldavia, Uzbekistan, Kirghizia has resulted in agreements on legal assistance and legal relations in civil, family and criminal matters. All 728 requests for legal assistance in 1997 and 529 requests up till July 1998 have been fulfilled.

### **3.8 External Policies**

#### **Trade and International Economic Relations**

Latvia continues to implement an open and liberal trade policy based on the principles of the WTO and relevant EU regulations, as well as those reflected in Latvia's bilateral trade agreements.

At present, Latvia has entered into the final stage of its accession to the World Trade Organisation (WTO). During the entire accession process, Latvia engaged in extensive consultations with the EU on harmonisation of its WTO commitments with those of the EU. Latvia was working with an awareness of its future obligations as a member of the Community. In particular, we note close co-operation and support of the EU in resolving issue on commitments of Latvia on audio-visual services.

In its accession negotiations to the WTO, Latvia has committed itself to implementing all the WTO obligations upon accession without any transitional period. An absolute majority of the WTO rules and regulations already constitute an integral part of Latvia's national legislation. Latvia has made a commitment to initiate negotiations on joining the General Procurement Agreement (GPA) by tabling an entity offer upon accession and also has joined sectoral initiatives for goods. Latvia expects to sign the Protocol of Accession to the WTO in the autumn of 1998 and subsequently become a Member of the WTO after complying ratification procedure.

In the context of its accession to the EU and to the WTO Latvia implements a consistent policy aimed at gradual trade liberalisation. Customs tariffs were reduced to zero or a 1% rate on many goods, and the average (non-trade-weighted) customs tariff rate for industrial goods declined to 4.5%. The last reduction of tariffs took place in January 1998. In respect to agricultural products, the average production-weighted tariff for all products was reduced to 34% in July 1997.

In its relations with international economic organisations Latvia is harmonising its activities, as well as undertaking commitments in full compliance with its obligations contained in the Europe Agreement and with due respect to its future obligations as a member of the EU.

Latvia continues to implement a trade policy directed towards becoming a party to the EU various preferential trade agreements. In 1997, a Free Trade Agreement with Turkey was concluded and on April 1998 the provisional application of the Free Trade Agreement with Poland began. Latvia is negotiating a Free Trade Agreements with Hungary and Romania and is planning to start negotiations with Bulgaria.

Co-operation among the Baltic States in implementing gradual liberalisation and regional integration policies is developing. A Baltic Common Economic Area is being introduced. Free trade in goods between Baltic States is already ensured, an agreement has been concluded on abolition of non-tariff barriers to trade and negotiations are proceeding on liberalisation of the services market.

Latvia is currently developing commercial defence legislation, for example, the law *On Safeguards* and law *On Anti-dumping*; this law will be drafted in compliance with the relevant EU regulations and WTO requirements.

## **Development**

Latvia has no specific allocation budget for development aid yet. However, Latvia has granted development aid on a case-by-case basis. For instance, in December 1996, the Latvian Government provided USD 110,000 aid to Bosnia-Herzegovina. No GSP schemes apply in Latvia, and no duty free access is granted.

## **Customs**

Since the beginning of transition, the Latvian customs system has continually been developing in order to absorb the positive features of EU regulations and international agreements. Taking into account that Latvia's eastern border will eventually form a part of the external EU border, continuous steps are being made to ensure the readiness of the Latvian tax and customs administrations to conduct efficient customs control on behalf of the EU, as well as to ensure a high degree of administrative co-operation with all the Member states.

A new *Customs Law*, which incorporates the requirements of EU customs legislation, the Kyoto Convention and the WTO Agreement, was adopted in June 1997. Adoption of necessary implementing provisions has just been completed. Regulations necessary for practical implementation of the norms on suspense arrangements and customs procedures with economic impact will come into effect on 1 January 1999.

Latvia is a party to several international conventions in the area of customs procedures. Latvia is a contracting party to the Customs Convention on the international transport of goods under the cover of TIR carnets since 1993. In October 1995, the Saeima adopted a law to accede to the International Convention on the Harmonised Commodity Description and Coding System. Recently the Saeima has ratified the Nairobi Convention. Joining the Kyoto and Istanbul conventions is planned. Latvia adopted the EU Combined Nomenclature in 1992, and a new version is in effect since 1 January 1998. Since 1 June 1997 Latvia participates in the European system of cumulating of rules of origin.

Joint customs checkpoints are being established with Estonia and Lithuania (one common checkpoint already operates at the Latvian-Lithuanian border, while five other points are in different stages of preparation). Pursuant to a recently concluded agreement between Latvia, Lithuania and Estonia, which was based on the EU/EBTA Common Transit Agreement, joint transit control will begin in the Baltic States from January 1999. This is the first step towards accession to the Common Transit Convention.

The Latvian State Revenue Service Customs Board has been carrying out a modernisation programme for two years. It covers legislation, organisation, procedures, training, computerisation and anti-smuggling operations.

To ensure that the customs procedures are in compliance with the respective EU norms, systems for customs value and post-importation audit, as well as a risk analysis system (TIMS), support system for guarantee mechanisms and customs debt administration system, are being introduced. The ASYCUDA++ system was selected by the Latvian Government for the computerisation of Customs revenue collection and statistics gathering process. Its installation is at a pilot stage and should be completely introduced by 2000.

Infrastructure of customs checkpoints, especially on the eastern border, is constantly being improved. The reform of State Revenue Service personnel management is being continued to ensure professionally competent, trained and motivated customs staff.

Co-operation in the fight against drugs and commercial contraband is based on bilateral agreements concluded by Latvia with Finland, Denmark, Sweden, and the Netherlands. Co-operation with other member states takes place under the framework of the 5th Protocol of Europe Agreement. Besides bilateral agreements are in force with Norway, Lithuania, Estonia, the Ukraine, Uzbekistan, Belarus and USA.

The Anti-smuggling Division of the State Revenue Service Customs Board, together with regional anti-smuggling units, takes part in many international activities, for instance, "FELIX" and drug routes identification in Europe. Both on its own and in co-operation with Border guards, the Division has undertaken numerous preventive measures against drugs transporting.

## **Common Foreign and Security Policy**

Latvia is a member of the United Nations, the OSCE, the Council of Europe and other international organisations. Latvia is an associated partner of Western European Union and member of the Euro-Atlantic Partnership Council.

Latvia contributes to increasing regional stability through active participation in the work of the Council of the Baltic Sea States and co-operation of the Baltic and the Nordic states.

Latvia does not have any territorial disputes with neighbouring countries; progress has been made in negotiations with Lithuania over sea border, and creation of common economic zone is under discussion, which gives hope of conclusion of agreement in near future. In order to secure the eastern border of Latvia, the Agreement between the Republic of Latvia and the Russian Federation on the state border already prepared by the commissions of both countries must be signed. Despite the fact that the Russian side has not expressed readiness to sign the agreement yet, Latvia will intensify the work at administration of the eastern border of Latvia.

The basic principles of co-operation of Latvia, Lithuania and Estonia with the United States have been elaborated. They are included in the US-Baltic Partnership Charter. One of the aims of the charter is to promote security of the Baltic States and their integration in the Euro-Atlantic security structures.

Peace-keeping forces of Latvia are participating in the NATO-led SFOR mission. Latvia's contribution to European security is also participation in the WEU-led MAPE mission in Albania.

Latvia has joined conventions on non-proliferation of nuclear, chemical and biological armaments, as well as has signed the Comprehensive Test Ban Treaty. Latvia has joined the NSG regime. Latvia has created an effective control of import and export of strategic goods. Lists of items under control are identical with those of the EU and in the export control we are following the EU guidelines.

In the sphere of security policy Latvia co-operates with the other Baltic states in four defence- related projects: Baltic Air Surveillance Network (BALTNET), Baltic Naval Squadron (BALTRON), Baltic Battalion (BALTBAT), and Baltic Defence College (BALTDEFCOL). The Baltic states and donor states have created Baltic Security Assistance Group to avoid overlapping of help and resources in the mentioned and other future security promoting projects in the Baltic states.

Several large "Partnership for Peace" exercises were conducted on Latvian soil, for example "Co-operative Best Effort '97," "Open Spirit," "Co-operative Baltic Eye '97," "Co-operative Batch '98," "Amber Sea '98." Latvia participates in more than 10 significant exercises annually to increase co-operation ability.

Latvia has offered Adazi base for conducting exercises of NATO and WEU states.

## **3.9 Financial Questions**

### **Financial Control**

Latvia has taken the necessary steps to ensure a properly functioning system of audit and financial control. The State Audit Office, an independent collegiate institution, is the central element of the system. The functioning of the internal control system is guided by the *Internal Audit Regulation for Ministries and other Central Government Bodies of Government*, adopted in Autumn 1996. Under these regulations all ministries have established internal audit structures.

The Latvian authorities recognise the importance of further development of internal control. Three international assistance projects are aimed at facilitating the strengthening of internal audit systems, including the PHARE project on public administration reform, which contains a component on audit and financial control.

Harmonisation of control procedures in the customs area is considered crucial in the context of European integration, taking into account that revenues from customs duties are part of the "own resources" of the EU. System specification for accounting for duties collected, including identification of customs debt and notification of the debtor, has been created and systems are now being developed to implement specification.

Necessary preparatory measures are being undertaken in connection with Pre-Structural Funds. The 23 March 1998 Decision of the European Council stipulated responsibilities of ministries in the process of preparation for Structural Funds. The principal role in the process was assigned to the Ministry of Finance which leads a special inter-ministerial working group. The group is responsible for preparation of necessary policy proposals both in respect to legislation and setting up new or reinforcing existing administrative

structures dealing with structural funds. Recently, a special co-ordination unit was established in the Ministry of Finance. Latvia will benefit from the Special Preparation Programme for structural funds under the PHARE facility.

### **Budgetary Implications**

Latvia is working on its current customs system, national accounts and statistics in order to align the establishing and monitoring own resources with EU regulations. As already mentioned in the previous section, system specification for accounting for duties collected has been created and systems are now being developed to implement specification in order to harmonise control procedures in the customs area. Moreover, efforts undertaken during the last years in the area of strengthening the process of budget planning and management resulted in creation of comprehensive and transparent budget projections.

Regulations on the development of annual budget are regularly perfected. A unified order of elaborating and submitting budget projections is enforced for any state institutions or undertakings. Elaborating and analysing consolidated state budget and planning the budget of local government, persistent steps are being made towards improving structure of the budget as well as design and content of the budget explanatory form. Law *On the State Budget* considers all financial sources (except donations) of state institutions. The law also regulates liabilities of the Government with respect to state debt and issued guarantees. Closer control over expenditures of bodies financed through the state budget is promoted. Special attention is paid to supervision of the expenditure side of local governments. To consider financial performance of local governmental structures on a complex basis, supervision of their financial activities is now being concentrated in a newly created unit.

### **C. ADMINISTRATIVE CAPACITY TO APPLY THE ACQUIS**

The Public Administration Reform agenda has the following key features:

- Each ministry has functions and structures appropriate to a modern state and a strategically planned budget;
- Competent and reliable staff are recruited and retained in the public service;
- Public institutions are managed effectively and in the public interest;
- The policy making and legislative process is rigorous and co-ordinated;
- Public institutions and staff are held accountable to the public;
- Local governments and their services are structured and provided with adequate resources so as to promote direct participation of citizens.

The Bureau of Public Administration Reform (BPAR) screens draft regulations and draft laws to ensure that proposals for changes to public functions, structures of public administration institutions, institutional status, and the status of civil servants or government employees are in line with the overall concept of public administration reform. In addition, the Bureau ensures that draft laws avoid conflicts of interest and situations of overlapping competencies both at institutional and management level. The European Integration Bureau is responsible for harmonising national draft legislation with the *acquis*.

Training for European integration has become especially important during the last two years. The School of Public Administration has provided senior and middle-ranking civil servants with training on EU institutions, policies, and decision-making procedures. 4055 civil servants were trained in 1997, 748 of them in EU matters and decision-making procedures. During 1997-98, within a PHARE-financed European Integration Programme, more targeted training was implemented for civil servants and sectoral experts. A database on European law and a library was established. A training programme for 78 staff managers was completed early in 1998.

An inter-ministerial working group has prepared draft Cabinet regulations *On Delegation of State Functions* to the non-governmental sector, based on an analysis carried out by the Bureau at the end of 1997. It should be noted that the draft law *On Public Administration Structure and Functions* was submitted to the Government for approval as a framework document for streamlining the institutional structure of ministries. It is expected to be approved by the Saeima in the beginning of 1999. In order to allow wider use of modern management practices in public administration, the Bureau of Public Administration Reform has drafted and submitted to the Cabinet a draft law *On Executive Agencies*. The State Chancellery has undertaken the development of a legal impact analysis with PHARE assistance in 1997-1998.

The Government adopted a National Programme for Prevention of Corruption in March 1998. Various institutions (e.g. the Police, the General Prosecutor's Office, the State Audit Office) have set out to implement the anti-corruption programme within their structures. A widely attended conference against corruption was held in June 1998 to increase public awareness.

In the area of public administration emphasis has been placed on development of internal audit functions in public organisations, introduction of annual reports on the accomplishments of public officials, and the elaboration of a code of ethics for public officials. A pilot-project on internal audit, involving the State Audit Office, the Ministry of Welfare and the Civil Service Administration (CSA), has been established. Within the PADBAS project (financed by the UK), training of 23 persons in auditing techniques will be completed in February 1999.

The Medium-term Strategy (Strategy 2000) and the Action Plan for Public Administration Reform was approved on 10 March 1998. Strategy 2000 describes the aims of reform in terms of fulfilling the public's right to a fast, cost-effective and high quality service from state institutions.

Earlier this year Latvia embarked on the Commission's Institution-Building and Twinning Initiative. The institution-building plan is linked to PHARE programming. Twinning projects will be finalised at the beginning of October 1998 by a Steering Committee. These projects are aimed at improving veterinary and phytosanitary control, improvement of wastewater management systems, and land planning for agricultural use. Internal Market capacity will be improved by a twinning project on State Aid Control, Public Procurement, and upgrading the data management system of the Central Statistical Bureau. Judicial reform is promoted by the improvement of internal administration of the judiciary and by the implementation of court judgements in civil and commercial matters.

The Ministry of Agriculture has established a Sanitary Border Inspection Unit which controls the conformity of import, export and transit cargo to veterinary, phytosanitary and hygiene requirements. Recently the Ministry reformed the European Union Rural Development Management Unit in order to make its structure more suited to work with pre-accession funds. The Ministry needs to assess current export promotion policy in order to introduce an appropriate export promotion agency and to re-enforce the market information network. The Ministry also plans to establish an institution responsible for state intervention in agriculture funds.

On 3 March 1998, the Government approved the concept on court bailiff reform. A working group has been set up to draft a new law *On Judicial Power* in order to codify the existing system of legal norms.

The Latvian Government is planning to join the Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data. The draft Law *On Personal Data Protection* provides for establishment of an independent monitoring institution, the State Data Inspectorate.

On 29 July 1997, a Co-ordinating Council for EU Education Programmes was established.

In 1997, an independent State Aid Surveillance Commission was established at the Ministry of Finance, consisting of thirteen members delegated by various institutions. The Competition Council (established in 1998) controls the enforcement of the law *On Competition*. The Council is a decision-making body and consists of five members who are nominated by the Government for a five year term.

In 1998-99, an institution that will manage deposit guarantee funds and an independent control institution for controlling public procurement procedures are due to be created. One of the key elements of financial market supervision is the plan for the establishment of a single financial market supervision authority.

Efforts undertaken during the last years in the area of strengthening the process of budget planning and management resulted in creation of comprehensive and transparent budget projections (see chapter 3.9.)

Forecasting capabilities which are especially important in budgetary planning have improved considerably. With support and advice of consultants under PHARE project, an up-to-date methodology of forecasting has been introduced. The combined effort of visiting consultants and local staff has resulted in creation of comprehensive macroeconomic model in Ministry of Finance.

Two years the state budget is worked out using the principle of programming, thus emphasising expected results and their cost efficiency. The Government selects the most important priorities and sets expenditure ceilings in the basic budget of each institution. Two times a year institutions report on their efforts to meet the targets.

Since preparation of the Medium Term Economic Strategy, co-operation among all the involved institutions has been strengthened in macroeconomic forecasting.

Establishment of the Financial Police of the State Revenue Service (SRS) in 1996, re-registering all VAT payers in 1996-1997, and approval of the single debt recovery methodology at the end of 1997 were the most significant events in improvement of tax administration in the 1996-97 time frame. A five-year SRS strategic plan (1998-2002) is prepared. In order to implement this plan, a separate plan for each unit is stipulated where certain performance criteria and indicators are defined.

A short term goal is the establishment of an internal audit unit for the whole SRS which will take over also the functions which are presently performed by Customs Internal Audit Unit. Recently an audit was performed in two territorial units of the SRS in order to produce an inventory of their functions as well as to identify weak

points in their work (this exercise was done by a specially formed group). In February 1998, document circulation in all SRS units underwent analysis. This analysis will help to simplify the process and make it more transparent. A proper system for risk factor analysis is being established. A vulnerability study concerning corruption was performed in all divisions of the SRS.

In order to improve the tax collection system, a program which would ensure overall SRS modernisation is being prepared in co-operation with the World Bank. The goals of the modernisation program are optimisation of utilisation of personnel and material resources, harmonisation of Latvian tax legislation with that of EU, and computerisation of the SRS in 2002.

In the process of implementation of the program, a three-level tax administration will be established whereby part of the functions presently performed by the main office of the SRS will be delegated to regional tax administration units. The program will consist of 28 projects.

The Ministry of Interior intends to establish the following institutions in the near future: an anti-corruption enforcement unit, a temporary placement point for asylum seekers at Riga Airport, a crisis management centre and information exchange network to connect border posts, a refugee affairs centre and a refugee appeals council. The temporary placement camp for illegal immigrants at Olaine will also be reinforced. Work will continue on the construction of an admission centre for asylum seekers at Mucenieki.

The draft of new *Telecommunications Law* has been completed. After the adoption of the new law, a new regulatory institution - the independent National Telecommunications Regulator - will be established. This will be the main driving force for reform in the telecommunications sector and will have the necessary administrative capacity and powers.

The Railways Administration and the Railways Technical Inspectorate will be established in accordance with the law *On Railways* adopted in April 1998.

The 3.7 million ECU PHARE project on Public Administration Reform is designed to refine and implement the measures developed in 1997-98.

#### **D. SUMMARY AND CONCLUSION**

In its *Avis* on Latvia's Application for Membership of the EU released on 15 July 1997 the European Commission recognised substantial achievements made by the Government of Latvia and society in the area of the European integration. *Avis* indicated also some problems and shortcomings which if not solved or eliminated would complicate the process of Latvia's accession to the EU. The Government of Latvia responded in a due way to the recommendations contained in the *Avis* by adopting relevant action plan in August 1997.

During the period since the publication of the *Avis* Latvia has made substantive progress in all areas where the European Commission indicated a need for additional effort and attention.

##### Political Criteria

Since Latvia's political institutions function properly and with demonstrated continuity and stability, the primary efforts of the Government and the *Saeima* were concentrated on the further measures to facilitate the integration of non-citizens into the Latvian society. The adoption of amendments to the *Citizenship Law* which brings it to the full conformity with the OSCE recommendations highlights the value Latvia has been placing on compliance with the Copenhagen's political criteria.

##### Economic Criteria

Latvia's ability to meet the economic criteria established at Copenhagen has been characterised by the following points.

Since publication of the *Avis* Latvia continued its progress towards the completion of market reforms. Further liberalisation of trade and land market took place. The economy is functioning in stable conditions and sustainable growth has been achieved. Considerable efforts have been made as to ensure that the practical implementation of legislation proceeds following its adoption. Follow-up action is being taken to ensure that all relevant regulatory bodies will be in place and will function effectively in the medium term. Privatisation is almost completed. The remaining state owned companies (in transport, energy infrastructure, communications or other strategic areas) will be privatised in nearest future.

Latvia already exhibits the capacity to cope with competitive pressure within the EU. A gradual shift in exports to goods with a higher proportion of value-added is taking place even as the share of capital goods imported is growing. Strong growth is observed in the banking sector and in other branches of financial services sectors. The modernisation of the agricultural sector is taking place.

#### Capacity to take on the obligations of membership

Since publication of the *Avis*, Latvia made further efforts to comply with the single market legislation. Considerable progress has been achieved in the areas of intellectual property rights, competition and personal data protection.

In the area of statistics Latvia is implementing continuously all relevant measures to ensure correspondence with EU requirements in the medium term. There is also significant progress in the strengthening of the administration of customs. Latvia is confident of its ability to practically implement the Union's *acquis* in this field.

Latvia is proceeding with enforcement of legislation in the area of environment and environmental protection. Even if full compliance with the *acquis* is expected in the long term, the efforts being made today demonstrate maximum efficiency of current and future spending in this field.

Latvia has made forward progress towards the construction of a comprehensive regional policy and the elaboration of instruments compatible to that of EU. Creation of the administrative structures (with support from the EU PHARE programme) enables Latvia to use with maximum efficiency EU regional and structural funds as soon as these policy instruments will cover Latvia.

Preparation of Latvia's agricultural sector for the full participation in EU Common Agricultural Policy is taking place. The stress and accent are on the creation of an administrative capacity to deal with structural instruments in this field. However further significant efforts are required to complete adaptation to the mechanisms of CAP.

Measurable progress has been achieved in the adoption of the Union's *acquis* necessary to remove the controls at borders between Latvia and member states of EU. To this end Latvia has established visa free travel arrangements with five EU member states. Further improvements in the control of Latvia's eastern border provides for the possibility to conclude the relevant agreements with EU memberstates being part of the Schengen accord already by the beginning of 1999.

In the area of justice and home affairs crucial legislation is steadily passing through the *Saeima* confirming Latvia's adherence to international legal instruments and their administrative enforcement. There is a clear vision of actions to be taken as to achieve full fledged participation in the justice and home co-operation.

#### 4. Administrative and legal capacity

The Government of Latvia is making significant efforts as to ensure that the Public Administration reform will lead in the medium term to firm establishment of the administrative structures necessary to apply and to enforce the *acquis* effectively.

#### **CONCLUSION**

In the view of all above mentioned, Latvia considers that since the publication of Commission's *Avis* sufficient progress has been made in satisfying the conditions of EU membership as defined by the European Council in Copenhagen as well as improving the area of shortcomings identified in *Avis*. Therefore Latvia will be able to assume the obligations of EU membership in the medium term.

## APs/NPAAs: Global Assessment and Implementation

After receiving the Commission's *Avis* in July 1997, the government of Latvia was already fully aware of the priorities for accession, as seen by the EC. These priorities have been consequently addressed by previous versions of the National Programme for integration into the European Union, by the Government's Action Plan and now by the Third National Programme.

Third National Programme for Integration into the European Union (NPAA) was approved by the Government in April 1998. This programme is Government's response to the Accession Partnership, incorporates the requirement for a National Programme for the Adoption of the *acquis*. Thus, the Programme indicates the specific commitments undertaken by the Government to deal with the operationalisation of priorities identified in the Accession Partnership document as well as the obligations set out by the Europe Agreement. The priority areas meant in the Accession Partnership are now specified as objectives to be reached in the short to medium term (according to the timetable in the Accession Partnership) and the NPAA provides with detailed "step by step" (operational) plans for implementation of each Accession Partnership objective. NPAA ensures the continuity of the integration process in Latvia, building upon work planned and carried out in the context of earlier programmes. The approach taken by the Latvian Government shows that preparations for integration into the EU are not limited only to the adoption of the *acquis* but also include activities to promote political stability, economic development and the integration of society in Latvia. These cover various priority measures, such as democratic control over military structures, reorganisation of prison system, prevention and combat of crime and corruption, ensuring of an effective asylum policy, promotion of the naturalisation process, informing the society about the European Integration process, completion of the privatisation process, etc. At present, there are no significant changes suggested to the priorities of the Accession Partnership.

The implementation of the NPAA is monitored by the European Integration Bureau and up to now no delays in implementation of the envisaged tasks have been observed. The monitoring mechanism will be further improved through the European Integration Information System (under development) - an electronic data base linking various governmental institutions. The data base will be Internet-based thus ensuring the transparency of the integration process.

The NPAA adds value to the process by developing and promoting a more comprehensive and integrated approach. The first two programmes were mainly concentrated on the legislative aspects of the integration process. NPAA is built on the recognition that to meet the "Copenhagen criteria" for membership it is necessary to put the task of adoption of the *acquis* in a relevant policy and administrative management context. NPAA states that: "approximation of legislation has become much more far-reaching than the simple transposition of Directives. It requires a planned approach to the management of the implementation and enforcement of new laws, rules and procedures".

In the NPAA priority areas and actions of the Accession Partnership were regrouped in four major strategic themes: reinforce the process of integration of Latvian society; develop the economy to cope with competitive pressures; the approximation of Latvian laws with those of the EU; improve administrative capacity.

Capable public administration and relevant policy co-ordination framework are the preconditions for the implementation of membership criteria, including the adoption of the *acquis*. As an integral part of the NPAA, section Improving the Administrative Capacity identifies a series of short to medium term priority needs and measures, covering public administration, agriculture, judiciary, economy, tax administration, environment etc. It sets the goals for institution building in Latvia.

It is important to stress, that the programme is a living document. It is used as a tool to measure the relevance of Phare and bilateral co-operation projects. The actions provided by the programme are taking place on a daily basis. This relates to all the envisaged forms of activities, legislative and institution building in particular. Intensity of the work can be witnessed on weekly basis, following the agenda of the Cabinet meetings.

The NPAA provides that the priorities of this Programme (and of the Accession Partnership) are estimated in terms of their implementation costs and budgetary requirements. The Programme covers the period from 1998 to 2000 and indicates implementation costs of each priority year by year. It also shows a source of financing - national budget, PHARE resources and bilateral assistance. The PHARE resources and bilateral technical assistance is generally intended to be used as a co-financing source rather than a sole financial contribution to the envisaged projects.

An assessment of budgetary implications has been done and reflected in the NPAA. However, it shows that there is a certain gap between the commitments made and the budgetary realities. As it is clear that for the time being no significant additional funding will be available to narrow the gap, in the future some rescheduling of the medium-term activities will be required. Recently, a meeting of a special commission with participation of the European Integration Bureau, Ministry of Finance and line ministries took place. Line ministries were

advised to bring their requests in concert with the primary priorities and resources. The Government has made a decision on future matching of planning the national budget and annual review of the NPAA and its financing. This will be an ongoing process and ensure that the Programme is a living document.

The NPAA is a strategic management document that has helped the Latvian administration to manage the integration process in a more operational and coherent way. To ensure further success of that programme several important issues will have to be addressed. First, it is essential that financial planning of the NPAA is further strengthened and linked in a more coherent way to planning of the National Budget. In fact, the NPAA has to become a simple framework for financing Latvia's accession including accommodation of resources from the Pre-Structural Funds. Second, the accelerating of institution building process is a significant factor for Latvia's accession to the EU. The NPAA already identifies its main objectives and sets necessary action plans. These will have to be widened in scope covering all the aspects of institution building. The Institution Building Plan, currently under development by the Public Administration Reform Bureau, upon its completion will be incorporated in the NPAA. Third, as the NPAA will be continuously reviewed and supplemented, it is planned to outline in a more detailed way the specific EC Directives for all the priorities of the NPAA. This will improve daily management of activities and reporting of progress in the line ministries.

As it has been demonstrated in the previous chapters, during the last year's time relevant progress has been achieved by Latvia in various sectors of the legislative and institution building activities. This has been particularly noted in two last meetings of the Sub-committee on approximation of law (October 1997 and July 1998) and in the meeting of the Association Committee in May 1998.

The most relevant developments in recent time are the new *Competition Law*, the law *On Control Over State Aid to Entrepreneurial Activity* in the area of public aids, the legislation package in the field of public procurement, the law *On Prevention of Use of the Financial System for the Purpose of Money Laundering*, the legislation package planned to be adopted this year in informatics field etc. (more detailed information see in Chapter 3. Ability to Assume the Obligations of Membership).