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Report to Congressional Requesters

July 2000

BOSNIA PEACE OPERATION

Crime and Corruption Threaten Successful Implementation of the Dayton Peace Agreement

GAO

Accountability * Integrity * Reliability

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Contents

Letter 3

Appendixes

Appendix I: Benchmarks for Measuring Progress in Implementation of the Dayton Peace Agreement 48

Appendix II: Bosnian Government and Judicial System Organization and Budgets 50

Appendix III: Bosnian, International, and U.S. Anticorruption Efforts 58

Appendix IV: Comments From the Department of State 62

Appendix V: Comments From the U.S. Agency for International Development 68

Appendix VI: Comments From the Department of Defense 71

Appendix VII: Objectives, Scope, and Methodology 72

Appendix VIII: GAO Contact and Staff Acknowledgments 73

Bibliography 74

Tables

Table 1: Budget Support Committed by the International Community for the Federation and Republika Srpska 39

Table 2: U.S. Executive Branch Benchmarks for Measuring Progress in the Implementation of the Dayton Peace Agreement 48

Table 3: 1999 Budgets for the Federation and Republika Srpska 56

Table 4: Major Bosnian, International, and U.S. Anticorruption and Judicial Reform Efforts 58

Figures

Figure 1: Destruction Caused by War 8

Figure 2: Geographic Boundaries of Bosnia, Its Constituent Entities, and the Federation's Cantons 10

Figure 3: Example of Material Used in Office of the High Representative's Public Awareness Campaign 22

Figure 4: Promotional Material for the Customs Hotline 24

Figure 5: WESTAR Operation in Progress and Seized Documents 25

Figure 6: Croat-Controlled Payments Bureau in Mostar 28

Figure 7: Holiday Inn Sarajevo 32

Figure 8: Bosnia's National Government Structure 51
Figure 9: Federation and Republika Srpska Entities' Government Structures 52
Figure 10: Federation Entity and Cantonal Law Enforcement and Judicial Systems 53
Figure 11: Republika Srpska Entity Law Enforcement and Judicial System 54
Figure 12: Revenue Sources in the Federation and Republika Srpska (1999) 55

Abbreviations

USAID U. S. Agency for International Development

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National Security and
International Affairs Division

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July 7, 2000

The Honorable Benjamin A. Gilman
Chairman
The Honorable Sam Gejdenson
Ranking Minority Member
The Honorable Douglas K. Bereuter
Member
Committee on International Relations
House of Representatives

The 3-1/2-year war in Bosnia killed over 250,000 people; forcibly displaced about 2.3 million; and damaged or destroyed the country's physical, economic, and political infrastructure. Representatives from Croatia, the Federal Republic of Yugoslavia, Bosnia's three major ethnic groups, and leaders of the international community signed the Dayton Peace Agreement in December 1995. The agreement was designed to, among other things, stop the warring factions from fighting, return people to their pre-war homes, and rebuild Bosnia's infrastructure—in short, to create a self-sustaining peace in a multiethnic Bosnia. The agreement also established the Office of the High Representative in Sarajevo, which assists and can direct the Bosnians in implementing the agreement.[1]

The international community, including the World Bank, the European Union, and the United States, committed more than $4 billion from January 1996 through December 1999 to finance the international effort to implement the civilian aspects of the agreement.[2] From January 1996 to December 1998 the primary focus of the civilian aspects of the Dayton Peace Agreement was on reconstruction efforts, but beginning in December 1998 the focus changed to building basic government

[1]For a full discussion of these events, including refugee returns and the international reconstruction effort, see *Bosnia Peace Operation: Pace of Implementing Dayton Accelerated as International Involvement Increased* (GAO/NSIAD-98-138, June 5, 1998) and *Balkan Suecurity: Current and Projected Factors Affecting Regional Stability* (GAO/NSIAD-00-125BR, April 24, 2000).

[2]Approximately $1 billion, of the over $4 billion in assistance funding was pledged by the United States. This does not include U.S. contributions to international organizations, such as the U.N. mission in Bosnia, or military costs. As of March 2000, the U.S. military costs for operations in Bosnia totaled approximately $10 billion.

institutions, such as the judicial system, and creating a free-market economy. The President has requested over $100 million for assistance to Bosnia in 2001.

The United States and the international community have succeeded in stopping warring factions from fighting and in rebuilding Bosnia's infrastructure. Now the goal of the international community, according to the Peace Implementation Council, is to strengthen the peace process and build democratic and market-oriented institutions.[3] To accomplish these objectives, Bosnian government officials are expected to increasingly assume greater independent responsibility for functions that had been undertaken or coordinated by the international community.[4]

In 1998, the U.S. government, the Peace Implementation Council, and the North Atlantic Council adopted benchmarks for evaluating implementation of the Dayton Agreement.[5] These benchmarks are intended to help determine when sufficient progress has been made in reconstructing Bosnia so that forces led by the North Atlantic Treaty Organization (NATO) can be withdrawn. Three of the benchmarks—the elimination of illegal institutions, the creation of a democratic law enforcement system, and the reform of the judicial system—are directly related to reducing the level of organized crime and corruption.[6]

You expressed concern about the impact of organized crime and public sector corruption on the efforts of the international community to rebuild Bosnia and meet the benchmarks for the withdrawal of NATO-led forces. As you requested, we examined (1) how organized crime and public sector corruption might affect the successful implementation of the Dayton Agreement in Bosnia, (2) whether the international community's anticorruption efforts have improved Bosnia's law enforcement and

[3]In December 1995, the London Peace Implementation Conference established the Peace Implementation Council to monitor and review progress in peace implementation. The Council's steering board consists of representatives from eight countries, the European Union, and the European Commission and is chaired by the High Representative.

[4]The report refers to any citizen of Bosnia as a "Bosnian," regardless of ethnic group.

[5]The North Atlantic Council is the political governing body of the North Atlantic Treaty Organization.

[6]For a full discussion of the benchmarks, see *Bosnia Peace Operation: Mission, Structure, and Transition Strategy of NATO's Stabilization Force* (GAO/NSIAD-99-19, Oct. 8, 1998).

judicial system and reduced corruption, and (3) whether international assistance resources are being safeguarded and whether such assistance is being used by Bosnia in place of domestic revenues lost due to crime and corruption.

Our review was based on studies, documents, and information provided by U.S. and international organizations involved in the implementation of the Dayton Peace Agreement. We attempted to identify instances in which the Bosnians were independently meeting the Dayton benchmarks without international edict or direction, as this is a main goal of the international community. (See app. VII for a more detailed discussion of our objectives, scope, and methodology.)

Results in Brief

Endemic crime and corruption is impeding the successful implementation of the economic, political, and judicial reform goals of the Dayton Peace Agreement. According to senior U.S. and international officials and numerous studies, corruption is impeding progress towards implementing the Dayton Agreement, and conditions for the complete withdrawal of NATO-led forces will not be met unless Bosnian officials make concerted efforts to address this problem. This, however, has not happened: crime and corruption continue to pervade Bosnia's political, judicial, and economic systems. U.S. and international officials further stated that this situation exists largely because Bosnian leaders from all ethnic groups have not demonstrated the political will to reform. However, State said some more moderate government officials have cooperated with the international community and others have cooperated under pressure. Numerous assessments have also concluded that the institutional structure for law enforcement and public accountability continues to be inadequate, precluding successful prosecution of government fraud, corruption, and complex white-collar crime. Moreover, other studies and international donors have concluded that the judicial system is threatened by corruption and is therefore institutionally incapable of effectively administering justice.

Bosnian, international, and U.S. anticorruption and judicial reform efforts have achieved only limited success in reducing crime, corruption, and political influence over law enforcement and judicial systems, according to U.S. and international reports and officials. While international efforts could provide needed supporting structures for the rule of law, most of Bosnia's leaders have chosen not to cooperate. Instead, Bosnian government efforts have primarily been to create committees and

commissions that have failed to become operational or measurably reduce crime and corruption. The Office of the High Representative has developed a strategy for coordinating international anticorruption efforts. However, these efforts have also achieved limited results to date, given the lack of high-level commitment to fighting crime and corruption within the Bosnian governments. U.S. efforts, led by the U.S. Agency for International Development (USAID), seek to curtail corruption through the elimination of communist-era financial control structures and the privatization of state-owned enterprises. Although efforts to replace state-owned financial structures with a private banking system are progressing, privatization efforts have been less successful. The U.S. ambassador to Bosnia suspended aid for the privatization effort in the Federation due to a lack of cooperation on the part of the Federation government.

U.S. and international donors have established procedures for safeguarding assistance to Bosnia, and there is no evidence that assistance is being lost to large-scale fraud or corruption. However, due to the fungibility of money, such assistance may be used to replace Bosnian domestic revenues lost to crime and corruption. Further, the United States has yet to recover approximately $900,000 in U.S. embassy operating funds and loan payments deposited in a bank that was involved in corrupt activities and is now bankrupt. Also, $340,000 in World Bank-provided funds were lost as a result of a procurement scheme perpetrated with fraudulent documents. Further, most of the $407 million committed by international donors to the Bosnian entity governments for general budget support (i.e., monies that are added to the entities' general revenues and are not earmarked for specific purposes) is not controlled or audited. Moreover, if the Bosnian governments strengthened the rule of law and identified ways to collect some or all of the hundreds of millions of dollars lost annually as a result of widespread tax and customs duty evasion, as estimated by the international community, budget support might not be needed.

Because senior Bosnian officials have not demonstrated the will to address the problem of crime and corruption and work toward a society based on the rule of law, we are recommending that the Secretary of State reassess the strategy for providing assistance to Bosnia. Such a reassessment should consider making changes in the type and amount of assistance provided, including the possible suspension of assistance to Bosnia, unless certain agreed-upon conditions are met. We also suggest that Congress may wish to require that State certify that the Bosnian governments have taken concrete and measurable steps to implement anticorruption programs and

significantly improve their ability to control smuggling and tax evasion before providing future assistance.

In commenting on this report, the Department of Defense specifically agreed with our conclusion that crime and corruption impedes the implementation of the Dayton Peace Agreement, and the Department of State and the Agency for International Development did not disagree with this conclusion. All three agencies believe, and we agree, that the international assistance effort has been successful in several areas, including the physical reconstruction of the country and maintenance of the cease-fire among the former warring factions. State disagreed with our recommendation and said that a reassessment of its approach to providing assistance to Bosnia is unnecessary because a reassessment was done in 1998 and the change in approach adopted at the time is still valid. Further, State said that conditioning the assistance the U.S. currently provides would be counterproductive because the assistance is designed to improve accountability and transparency and promote the rule of law, assistance which is unwelcome by the hard-line obstructionists who oppose the Dayton Agreement. The U. S. Agency for International Development echoed this concern in its comments. Despite these disagreements, we believe a reassessment of the strategy for accomplishing U.S. objectives in Bosnia is warranted. We found no evidence that State's reassessment process addressed the underlying causes of corruption and a lack of reform, namely the continued obstructionist behavior of the hard-line nationalist political leaders and others who State acknowledged have obstructed reform efforts promoted by the international community. It is widely recognized by U.S. and international officials that so long as the hard-line obstructionists retain control in Bosnia, the ability to achieve the Dayton Agreement objectives and the ultimate withdrawal of NATO-led troops is unlikely. A reassessment of the current strategy may identify a course of action more likely to achieve U.S. objectives.

Background

Bosnia was one of six republics of the former communist state of Yugoslavia. Its social, political, legal, and economic systems were developed and shaped by 45 years of communist rule. During 1991-92, Yugoslavia collapsed as four of its constituent republics declared independence. In Bosnia, nationalist parties of the Croats, the Serbs, and the Muslims became the local successors to the communist party and assumed control of the social, political, and economic systems of the country. The war between these ethnic groups solidified their parties'

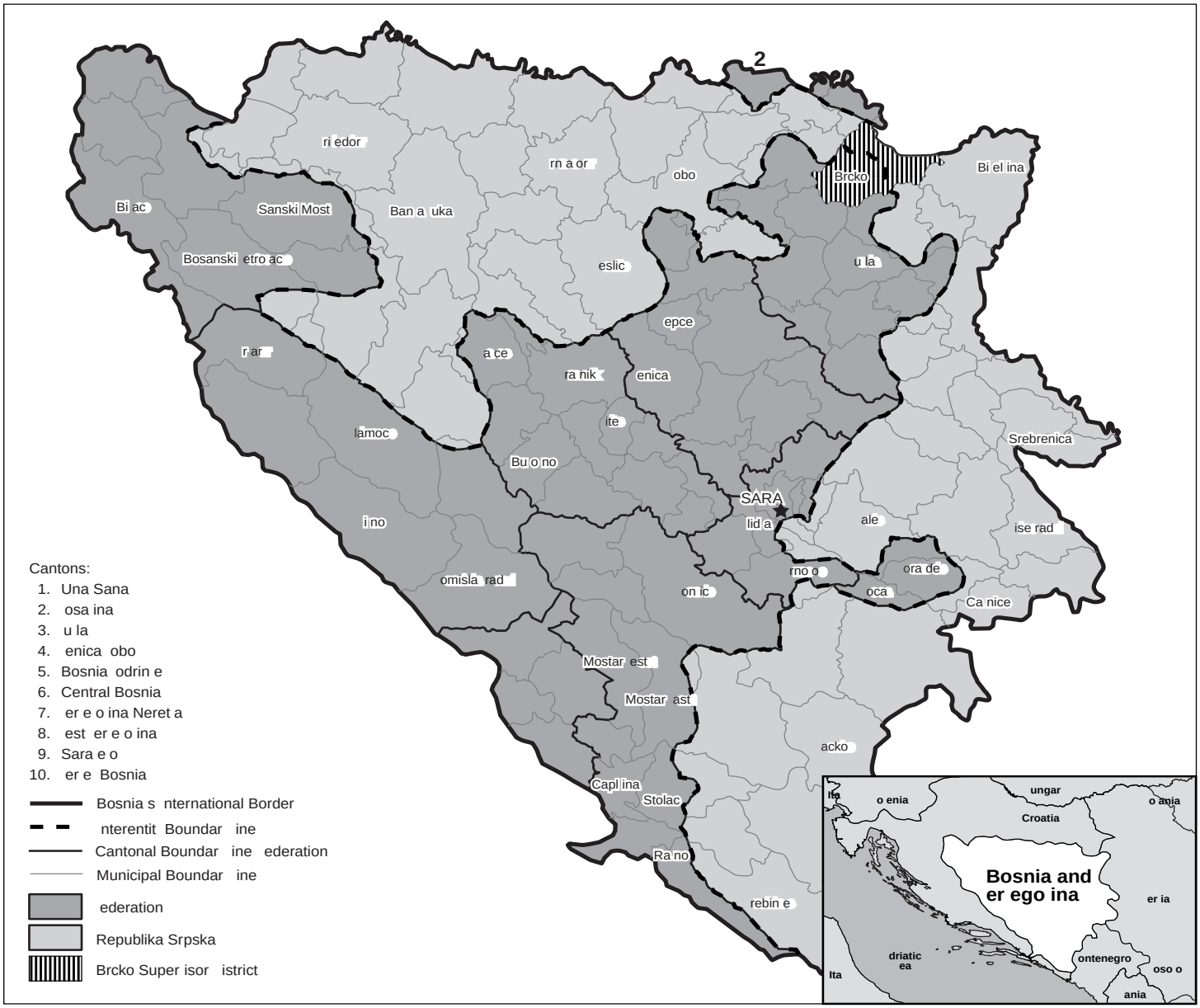
authoritarian power. (Fig. 1 contains pictures of the destruction caused by the war.)

Figure 1: Destruction Caused by War

Source: GAO.

With the signing of the Dayton Peace Agreement in December 1995, the war ended, the Bosnian national government was created, and the two entities created during the war were recognized. The competing nationalist parties control the national government, and each of the two entities—the Bosnian/Croat Federation and the Republika Srpska. Each entity has its own government, army, and police force. The Federation is further divided into 10 cantons, each with its own government. The Croat-controlled cantons constitute a de facto third entity because they do not recognize Federation law and are run by a number of parallel institutions such as payments bureaus, which control financial transactions in Bosnia. At Dayton, the parties were unable to agree on which of Bosnia's ethnic groups would control the strategically important area in and around the city of Brcko. The agreement called for an arbitration tribunal to decide this issue. The tribunal decided, on March 5, 1999, to make Brcko a self-governing neutral district. Figure 2 illustrates the geographic boundaries of Bosnia, its constituent entities, and the Federation's cantons. (App. II contains organization charts of Bosnia's national and entity governments and law enforcement and judicial systems.)

Figure 2: Geographic Boundaries of Bosnia, Its Constituent Entities, and the Federation's Cantons



Source: United Nations. Boundaries are as of April 2000.

Note: Cantons 1, 3, 4, 5, and 9 are under Bosnian Muslim control. Cantons 2, 8, and 10 are under Bosnian Croat control. Cantons 6 and 7 are mixed. Republika Srpska is under Bosnian Serb control.

A unique aspect of the Dayton Agreement was the establishment of the Office of the High Representative. This Office has significant powers, including the power to impose laws and remove any government official that engages in anti-Dayton Agreement activities. A number of international organizations, including the United Nations, the European Commission, the Organization for Security and Cooperation in Europe, the World Bank, and the U.S. Agency for International Development, provide technical assistance targeted at, among other things, judicial reform and economic development to further the implementation of the agreement. The NATO-led Stabilization Force supports these international agencies' efforts by creating secure conditions for the conduct of civilian-led reconstruction efforts in addition to implementing the military aspects of the Dayton Agreement.

Bosnia is undergoing simultaneous transitions from war to peace, from communism to democracy, from a government-run economy to a market economy, and from a rural population to an urban population. To implement the provisions of the Dayton Peace Agreement and help Bosnia through these various transitions, the international community developed a comprehensive $5 billion, 5-year international assistance effort. To assess Bosnia's progress in implementing the Dayton Agreement and determine when implementation can continue without a major NATO-led military force, the U.S. government established 10 benchmarks in March 1998. The North Atlantic and Peace Implementation Councils adopted similar benchmarks.[7] (The benchmarks and Dayton Peace Agreement are described in app. I.) The benchmarks are as follows:

- Military stability: Maintain Dayton Agreement cease-fire.
- Persons indicted for war crimes: Cooperation with the International Criminal Tribunal for the former Yugoslavia, leading to the transfer of indicted war criminals to The Hague for trial.
- Brcko: Implementation of the Brcko Arbitration Tribunal's Final Award that was issued on March 5, 1999.

[7]NATO agreed to benchmarks parallel to the U.S. benchmarks as part of its approval of the Stabilization Force military plan (OPLAN 10407). According to the plan, NATO's desired end state is an environment adequately secure for the "continued consolidation of peace" without further need for NATO-led military forces in Bosnia. The Peace Implementation Council established a set of conditions that must be realized for a self-sustaining peace to take hold in Bosnia. The Council did not link improvements in conditions to a withdrawal of the NATO-led force from Bosnia.

- Elections and democratic governance: National democratic institutions and practices.
- Media reform: A regulated, independent, and democratic media.
- Displaced person and refugee returns: A functioning, phased, and orderly minority return process.
- Illegal institutions, organized crime, and corruption: The dissolution of illegal pre-Dayton Agreement institutions.
- Judicial reform: An effective judicial reform program in place.
- Public security and law enforcement: A restructured and democratic police force in both entities.
- Economic development: Free-market reforms.

Some of the benchmarks have largely been met, such as maintaining the cease-fire and implementing the Brcko Arbitration Tribunal's Final Award, and some progress has been made in meeting other benchmarks. However, according to the High Representative, none of the progress achieved to date is self-sustaining. Further, although reducing crime and corruption is a separate benchmark, the pervasive illegal activity affects progress in meeting many important benchmarks, achieving U.S. policy objectives in Bosnia, and the Dayton Peace Agreement's ultimate goal of a self-sustaining peace.

Crime and Corruption Are Pervasive

U.S. and international organization officials, as well as numerous published reports, agreed that organized crime and corruption pervade Bosnia's national political parties, civil service, law enforcement and judicial systems, and the economy.[8] Bosnia's nationalistic political parties control all aspects of the government, the judiciary, and the economy, and in so doing maintain the personal and financial power of their members and authoritarian control over the country. The High Representative has stated publicly that corruption in Bosnia is endemic and progress in achieving the goals of the Dayton Agreement is often so incremental as to be almost invisible, especially to the outside world. Further, in testimony before the House International Relations Committee in September 1999 the State Department's Director of Bosnian Implementation stated that "corruption is undeniably one of the prime obstacles to achieving the goals set forth at

[8]Corruption in Bosnia was defined by the High Representative as, among other things, "abuse of office for private gain including awarding contracts for public works projects as political or economic favors; misuse of public funds and donations; disrespect of laws such as the Procurement Law; tax evasion; bank fraud, etc."

Dayton." With crime and corruption pervading every aspect of Bosnian society and the economy, the Deputy High Representative, the Supreme Allied Commander Europe, and the U.N. Special Representative to Bosnia told us that the benchmarks for evaluating the implementation of the Dayton Agreement cannot be met.

Political Parties Control Bosnia

The current political power structure, like the former Yugoslavian communist system, governs by the rule of party rather than the rule of law, with an absence of accountability and transparency according to, among others, U.S., Office of the High Representative, and U.N. officials in Bosnia. As a result, the political parties control public administration, the judiciary, and the economy. In January 2000, the U.N. Special Representative to Bosnia stated before the Legal Affairs and Human Rights Committee of the Council of Europe[9] that

> "war-time underground networks have turned into [political] criminal networks involved in massive smuggling, tax evasion, and trafficking in women and stolen cars. Some politicians play the nationalist card to mask their commitment to develop state institutions. For them, public accountability and personal responsibility are notoriously absent."

In his presentation to the council the High Representative stated that

> "the main political parties still rule Bosnia along ethnic lines. They are interested in political power, not because it allows them to serve the interests of all citizens of Bosnia, but because it allows them to pursue their own ethnic agendas."

According to the International Crisis Group,[10] the registration system for political party candidates has consistently failed to investigate the backgrounds of party candidates for anything other than whether they are citizens and whether the International Criminal Tribunal for the Former Yugoslavia has indicted them.[11] The result is that corrupt local officials

[9]The Council of Europe is an international organization based in Strasbourg, France. Its main role is to strengthen democracy, human rights, and the rule of law throughout its member states. The defense and promotion of these fundamental values is no longer simply an internal matter for governments but has become a shared and collective responsibility of all the countries concerned.

[10]*Rule Over Law: Obstacles to the Development of an Independent Judiciary in Bosnia and Herzegovina*, International Crisis Group (Sarajevo, July 5, 1999). The International Crisis Group is a private, multinational organization committed to strengthening the capacity of the international community to anticipate, understand, and act to prevent impending crises and conflicts.

occupy elected positions with a stamp of approval from the international community, an uncomfortable situation that has been documented by such international groups as Human Rights Watch.[12] Some international observers, including the International Crisis Group, believe that the inability of the international community to prohibit suspected criminals from running for public office is one of the major reasons why organized crime is so prevalent today.

According to the international officials we spoke to, including the U.N. and NATO-led Stabilization Force, a complex web of interrelationships exists between organized criminals and government officials. In congressional testimony before the House Armed Services Committee, in February 2000, General Wesley Clark, Supreme Allied Commander Europe, stated that the international community has to remove corrupt leaders who cooperate with criminal elements in order to eliminate impediments to economic growth and refugees' return.[13]

U.N. and U.S. Embassy officials in Bosnia and published reports indicate that during the war individuals rose to powerful positions in the Bosnian government by engaging in corrupt and/or criminal business activities, including illegal financial transactions and smuggling. International Crisis Group and European Stability Initiative[14] reports indicate that some of these individuals have continued to conduct illegal activities but have not been prosecuted because they kept their side supplied with arms and food during the war. Having used illegal networks for military and economic

[11]The Organization for Security and Cooperation in Europe administers the registration system with instructions from the Provisional Election Commission. The Organization is a regional security organization whose 55 participating states are from Europe, Central Asia, and North America. The Commission was created by the international community and is responsible for, among other things, establishing electoral rules and regulations and organizing election monitoring to ensure free and fair elections. The Tribunal for the Former Yugoslavia has the power to, among other things, prosecute persons responsible for serious violations of international humanitarian law in the territory of the former Yugoslavia since 1991.

[12]Human Rights Watch is a nongovernmental organization dedicated to protecting the human rights of people around the world.

[13]The Supreme Allied Commander Europe has military authority over NATO-led forces in Bosnia.

[14]The European Stability Initiative is a nonprofit think tank focusing on South Eastern Europe. It provides policymakers with timely, high-quality analyses of political, social, and economic developments in the region.

ends during the war, political parties are now inseparable from criminal organizations. Furthermore, the European Commission's Customs and Fiscal Assistance Office (hereafter referred to as the Customs Assistance Office)[15] and entity customs administrations conducted investigations in 1997 and 1999 showing that certain smuggling operations could have been successful only with the participation of customs officials. In addition, according to the Department of State, criminal elements involved in narcotics trafficking have been credibly linked to public officials. The proceeds from the narcotics trade are widely believed to support parallel institutions maintained by ethnic extremists. However, there have been no legal actions against public officials for narcotics-related offenses.[16]

Corruption Pervades Public Administration

Transparency International documented the culture of lawlessness and the lack of institutional authority that pervades Bosnian society during fieldwork conducted in 1998.[17] Local polling firms that conducted a survey of over 2,800 individuals for the State Department in October 1999 found that 50 percent or more of all three ethnic groups believe that corruption is prevalent among the central government, local governments, and business people.[18] The vast majority of legal abuses occur within the Bosnian public administration system, where government officials, appointed by local political party bosses, screen out public complaints and engage in corrupt activities such as taking bribes. For example, as reported by the International Crisis Group, the ruling parties appoint high-ranking officials—whose only qualification for the most part is party loyalty.[19]

[15]The Customs Assistance Office was established in 1996 to help Bosnia form a coherent customs system at the national and entity levels. *Loss of Revenue Within the Transit System and Failure of Control, A Report by the European Commission Customs and Fiscal Assistance Office,* (Sarajevo: Oct. 24, 1997) and *Report on Importations for State Directorate for Strategic Reserves, Sarajevo and State Directorate for Strategic Reserves,* Mostar, A *Report by the European Commission Customs and Fiscal Assistance Office* (Sarajevo: Oct. 24, 1997).

[16]*International Narcotics Control Strategy Report, 1999,* Released by the Bureau for International Narcotics and Law Enforcement Affairs, U.S. Department of State (Washington, D.C., March 2000).

[17]Transparency International is a nongovernmental organization dedicated to increasing governmental accountability and curbing international and local corruption.

[18]Opinion Analysis, Office of Research, U.S. Department of State, December 1999.

[19]*Rule of Law in Public Administration: Confusion and Discrimination in a Post-Communist Bureaucracy,* International Crisis Group, (Sarajevo: Dec. 15, 1999).

Office of the High Representative and other officials told us that Bosnian officials misuse their positions at all levels of government, and sanctions are rarely imposed unless the international community intervenes. In Tuzla, the former cantonal prime minister and other officials have been investigated by the Federation's Financial Police for misusing their positions.[20] The international community has closely monitored this case. In March 2000, the former cantonal prime minister was sentenced to 2 years and 2 months in jail for the misuse of his position and government funds. However, according to a U.S. official responsible for providing training in law to Bosnian prosecutors and judges, Bosnia has no truth-in-sentencing laws. Consequently, it is difficult to ensure that the officials prosecuted in Tuzla or other criminals serve their sentences. U.N., Office of the High Representative, and U.S. officials we spoke to could not cite a single case in which a high-level official had been jailed on a corruption-related charge prior to the Tuzla case.[21] In fact, of the 30 economic crime cases sent to the Tuzla municipality prosecutor's office in 1998 and 1999, 3 were dismissed and 27 were pending.

Office of the High Representative and U.S. officials, among others, stated that bribery is a systemic means for poorly paid corrupt public officials to supplement their income. The International Crisis Group and USAID have documented the pervasive use of bribery. For example, USAID conducted a survey in 1999 of Bosnian business people and found that they routinely pay bribes to receive government contracts, obtain government loans, and avoid being closed by government inspectors.[22] According to the International Crisis Group, the pervasiveness of nepotism and the tendency to use contacts to achieve one's rights has become the norm. Almost every segment of administrative procedure is based on a grid of connections, from friendships to those of a political and often criminal nature. For example, through its survey, USAID found that business people routinely

[20]The Financial Police are part of the Ministry of Finance and have the authority to investigate government organizations and government-owned enterprises.

[21]According to the Office of the High Representative's Anti-Fraud Unit, the international community has not attempted to determine the universe of corruption-related cases being pursued by the entities' legal authorities.

[22]*Payments Bureaus in Bosnia and Herzegovina: Obstacles to the Development and a Strategy For Orderly Transformation,* USAID, Sarajevo, Bosnia and Herzegovina (Sarajevo: Feb. 15, 1999).

use connections within the governments' financial control organizations to circumvent controls and obtain financial information on competitors.

Law Enforcement Favors Those in Power

Bosnia has almost no history of democratic governance; consequently, law and order has been imposed on the people by whoever wielded power. According to the U.N. International Police Task Force, Bosnia has one police officer for every 250 citizens compared to one for every 500 citizens in the United States. However, these police officers' allegiance is often to ethnic political parties rather than to the public. For example, through its audits of Bosnian police operations in 1998 and 1999, the U.N. mission in Bosnia found that there was no separation between the Bosnian Croat army, controlled by the Croat nationalist party, and the local police in Stolac. The army was operating out of the Stolac police station.

In November 1999, the Office of the High Representative removed the minister of the interior of one canton for, among other things, repeated failure to take disciplinary action concerning unfit police officers despite court verdicts of serious criminal offenses. According to U.N., European Union, and other international officials we spoke to, police in some areas continued to work for local party officials and were used to protect the business interests of these individuals, intimidate citizens, and prevent the return of refugees. For example, a Bosnian Croat police officer killed a Bosnian Muslim during an attempted visit to a cemetery in Croat territory. Although the incident was photographed, the police officer received a suspended sentence for using excessive force, and the judgment stated that it must be remembered that he was fighting for his country.

Judicial System Is Inadequate

An inadequate judicial system precludes successful prosecution of government fraud, corruption, and complex white-collar crime. According to the Office of the High Representative's Judicial Reform Strategy, the judicial system is institutionally incapable of effectively administering justice, and political involvement occurs at many stages of the judicial process. According to U.N., U.S., and Office of the High Representative officials we spoke to, there are good individuals throughout Bosnia's judicial system, but it would be virtually impossible to have all the parts of the system work properly in the same case. Ministry of Interior officials in Republika Srpska told us that the justice system in the republic was not functioning and that their work is futile because the Ministry of Justice does not take action on the investigations they conduct. A Bosnian legal scholar stated that Bosnia has laws that could be used to prosecute

organized crime and corruption. However, these laws are not being applied, and political influences over the courts prevent cases from being heard.

According to the Office of the High Representative, the International Crisis Group, the U.N. Mission in Bosnia, and other organizations, the selection of judges in Bosnia is the product of political patronage, and judges' salaries are controlled by political structures. A poll conducted by a national Bosnian daily newspaper in April 2000 found that approximately 73 percent of the respondents in three of Bosnia's largest cities did not believe the court system was independent. Under the current structure judges, prosecutors, and all who are involved in the judicial process are vulnerable to political, ethnic, and economic pressures, including physical threats and beatings. According to international officials, local criminal leaders, many of whom are closely linked to ruling political parties, are ready to threaten judges, prosecutors, police officers, lawyers, or witnesses with violence, or even death, to act in a particular way. For example, in one case, well-known gangsters, in an effort to intimidate a judge, monitored the trial of one of their associates to ensure he received a "fair trial." The defendant, one of the first people indicted by the International Criminal Tribunal for the former Yugoslavia, was acquitted of murder. The close relationship between the political power structures and organized crime and corruption results in pressure being placed on judges and prosecutors to overlook the crimes of known criminals and those in power. One well-known criminal was arrested numerous times on various offenses before he was convicted.[23]

In May 2000, the High Representative removed the governor and prime minister of one of the cantons in the Federation due to their persistent abuse of power. Under their governance, the canton was characterized by a dysfunctional judicial system and lack of respect for the rule of law. These officials refused to appoint competent prosecutors and judges for the canton. According to the High Representative, police in the canton applied different standards of justice and law enforcement for citizens based on their ethnic origin. Since all corruption cases necessarily involve public officials, a judiciary reliant upon the political party in power will always be questionable.

[23]The conviction resulted from the beating of a police officer.

Corruption's Effect on the Economy

A large portion of the Bosnian economy is underground, public utilities engage in corrupt practices, and international investment is stymied by pervasive corruption. In November 1999, Bosnia's three presidents appeared before the U.N. Security Council and acknowledged that corruption and the lack of transparency in government operations were serious problems that have blocked Bosnia's economic development.[24] According to USAID, about 50 percent of Bosnia's gross domestic product in 1999 was generated by the underground economy, and customs and tax evasion are endemic. In addition, a number of public companies, including electric, water, and telephone companies, are monopolies that exercise power over citizens in a variety of ways.[25] All three types of utility companies set arbitrary prices and follow the guidelines and fund the operations of local politicians and political parties that control the utilities in their areas. According to officials in Bosnia, these companies are subject to political abuse and present a formidable tool in preventing minority refugees' return.

The most common complaint from business professionals in Bosnia is the existence of pervasive corruption, according to a USAID survey of businesses and an International Crisis Group report. Corruption raises the cost of doing business so much that investors are unable to accurately forecast costs and cash flows. This leads to a situation in which the return on investment is no longer profitable and continuing operations is impossible. Consequently, private investment in Bosnia in 1997 and 1998 ($160 million) was insignificant, thus stalling efforts to rebuild a self-sustaining economy. One indication of how bad the climate for investment in Bosnia is can be seen by the lack of interest by potential investors in the European Commission's special trust fund to insure investments in Bosnia. Although established more than 2 years ago, as of March 2000, the fund had not yet registered its first investment. The U.N. Special Representative to Bosnia believes that corruption is the biggest single obstacle to the achievement of a self-sustaining economy in Bosnia. Further, international officials, including the NATO-led Stabilization Force

[24]The three members of the Bosnia joint presidency accepted the invitation of the U.N. Security Council to appear before it on the eve of the fourth anniversary of the Dayton Peace Agreement. The U.N. Security Council consists of 5 permanent members and 10 nonpermanent members and is responsible for the maintenance of international peace and security.

[25]Each ethnic group has its own electric, water, and telephone company. These companies exercise monopoly powers in their own ethnic areas.

Commander, believe that the primary obstacle to refugee returns is the poor economy.

Anticorruption and Judicial Reform Efforts Have Been Largely Unsuccessful

Over the last 4 years the Bosnians, the international community, and the United States have initiated a wide range of reform efforts to address the immediate effects of crime and corruption. In addition, the international community has implemented other efforts that attempt to strengthen the weak judicial systems and to build the capacity within Bosnia to fight these problems. The efforts, while helping to provide the building blocks for judicial reform, have had limited success in reducing crime, corruption, and political influence over law enforcement and the judiciary. (For a more complete listing of anticorruption and judicial reform efforts in Bosnia see app. III.)

Bosnian Efforts Have Not Reduced Corruption

The Bosnian and entity governments have initiated five anticorruption committees, commissions, or groups. However, according to U.S., Office of the High Representative, and other international officials, these efforts have achieved little success, and the political will of government officials is rarely demonstrated. The five initiatives are as follows:

- In 1997, the Federation's House of Representatives created a commission to investigate corruption. According to the Office of the High Representative, the commission became operational in 1998 but was unsuccessful because it lacked government cooperation.
- The chairman of the Bosnian presidency created an anticorruption commission in 1997 to look into fraud and corruption, but it never became operational.
- In September 1999, the Federation established a commission of international legal experts to combat corruption and work with international organizations to set up a regime that promotes transparency in government operations. The commission's report, published in February 2000,[26] found that among other things, corruption is a serious problem in the Federation and is caused by a number of factors, including Bosnia's communist past and its current tax system.

[26]The commission focused on the Federation because Republika Srpska declined to participate. The commission's mandate was to, among other things, examine the nature and causes of corruption in the Federation and recommend measures to improve its anticorruption efforts.

The commission recommended the creation of a special anticorruption task force, led by a special prosecutor, that would lead and direct the selection, preinvestigation, and trial of major cases of corruption. In April 2000, officials in the Federation began discussions to start an anticorruption effort headed by the prosecutor's office.

- In November 1999, the entities' prime ministers agreed to establish an interentity anticorruption group. As of May 2000, this group had not been established.
- In December 1999, the Federation's parliament began efforts to develop an anticorruption strategy. The working groups for this effort intend to analyze the Office of the High Representative's anticorruption strategy and then develop their own strategy and implementation plan. As of March 2000 the plan was completed and had been sent to the Federation parliament for review.

According to the Office of the High Representative, there are no formal anticorruption efforts in Republika Srpska. Further, the U.S. Ambassador to the United Nations stated in a November 1999 address to the U.N. Security Council that "the governments of Bosnia could do far more to fight corruption than they had over the past 4 years. There must be a stronger fight against the forces of darkness; the murderers, the fascists, the crooks, the thugs."

Non-U.S. International Anticorruption Efforts Have Had Limited Success

International organizations have instituted a range of efforts that have achieved limited success in the fight against crime and corruption. However, international officials, including the Office of the High Representative and the Customs Assistance Office, among others, stated that without their continued involvement, the Bosnians would not continue these efforts.

The Office of the High Representative initiated a number of anticorruption efforts in 1999 and 2000, including publishing an anticorruption strategy, establishing a public awareness campaign, and assisting the Bosnians with specific corruption-related cases. These efforts are lead by the office's Anti-Fraud Unit. In February 1999, the unit published an anticorruption strategy that brought together the major anticorruption activities of the international community. In September 1999, the High Representative established an Anticorruption and Transparency Group comprised of individuals from the international agencies working in Bosnia to coordinate the international community's efforts to implement the strategy. In March 2000, the Anti-Fraud Unit started an anticorruption public awareness

campaign. The first phase of the campaign includes a series of radio jingles, television cartoons, posters, and comic strips. Figure 3 contains examples of the material used in the campaign.

Figure 3: Example of Material Used in Office of the High Representative's Public Awareness Campaign

Translation: Let's Fight Corruption Through The Ballot Box!

Translation: Demand Faster and Simpler Public Services Lets Fight Corruption! (Paper Pushing Ministry)

Source: Office of the High Representative. Translation by U.S. Embassy, Sarajevo.

The unit is also assisting the Bosnians in the investigation and prosecution of significant fraud, economic crime, and corruption cases. This approach is intended to help improve the investigative and prosecutorial capabilities of the Bosnians. For example, the unit is working with Bosnian officials on significant corruption cases in Tuzla, Bihac, and Sarajevo. Although the unit is tasked to assist local authorities in investigating fraud and corruption and prosecuting the perpetrators, it does not have the power to undertake independent investigations or law enforcement actions.

According to the United States, United Nations, International Crisis Group, and other international officials in Bosnia, anticorruption efforts have not had a major impact, in part because Bosnians are not equal partners in the effort. Some officials further stated that the anticorruption strategy is more a recitation of existing international efforts rather than a strategy and that although the work of the international community is collegial, it is not truly coordinated.

The anticorruption effort led by the Customs Assistance Office and funded by the European Commission is considered to be the most successful anticorruption effort. The Office has assisted in establishing needed customs legislation and customs services at the entity level.[27] Investigations conducted and systems put in place by the Office have identified incidents of corruption and illegal activities that have resulted in the loss of millions of dollars in customs duties and tax revenues. In addition, customs officials perpetrating illegal activity have been exposed. According to the Republika Srpska Customs Administration, 45 employees have been dismissed and criminal proceedings are pending against 30 others.

The Customs Assistance Office set up telephone hotlines in September 1999 to allow citizens to report illegal activities in both the Federation and Republika Srpska. During the first 2 months of operation in Republika Srpska, 1,250 callers provided leads that led to the seizure of smuggled goods worth $1.5 million. (Fig. 4 is an example of the promotional material used to inform citizens about the hotline.) Although the Office's work is considered successful, officials there said that the entity customs

[27]In Bosnia, customs policy is developed at the state level, but customs administration and enforcement are the responsibility of each entity. Each entity has its own account for the customs revenue collected, and the revenue belongs to the entity where the goods are cleared.

administrations would not continue to function if the office's work were terminated today.

Figure 4: Promotional Material for the Customs Hotline

Source: Customs Assistance Office. Translation by U.S. Embassy, Sarajevo.

In order to assist in the implementation of the Dayton Agreement, the North Atlantic Council tasked the commander of the NATO-led Stabilization Force, through the Supreme Allied Commander, Europe, with the mission of providing a continued military presence in order to deter renewed hostilities, contribute to a secure environment, and help stabilize the peace. In keeping with this mandate, the NATO-led force established an

office of the inspector general to help eliminate fraud and corruption in the entities' armed forces. The focus of the office's investigations is professional military ethics and leadership concerns. NATO officials responsible for establishing the inspector general's office told us that to date, the investigations have led to the "removal, reassignment, or suspension of non-compliant" personnel. Those that have been reassigned have been transferred out of command posts to administrative assignments. In addition, the NATO-led force has initiated broader anticorruption efforts, mainly for force protection purposes. In October 1999, the force conducted Operation WESTAR, a major raid on Bosnian Croat covert intelligence facilities that resulted in the seizure of large quantities of weapons, pirated software, counterfeiting equipment, and intelligence information. (Fig. 5 shows the WESTAR operation in progress.) NATO officials stated that the confiscated material clearly indicates that Bosnian Croats were involved in anti-Dayton Agreement and organized criminal activities. State Department officials hope that the evidence gathered during this operation can lead to progress in overcoming nationalistic resistance to the Dayton Agreement and the prosecution of specific individuals on corruption-related charges.

Figure 5: WESTAR Operation in Progress and Seized Documents

Source: NATO.

The World Bank's initiatives to help Bosnia implement a modern public financial management system include, as primary objectives, the promotion of transparency and accountability in the Bosnian budgeting process. It also implemented a study in May 2000 to determine the root causes of corruption in the country. Despite these ongoing efforts, International Monetary Fund, World Bank, and other officials we spoke to stated that the entity budgets still lack transparency. The Organization for Security and Cooperation in Europe has implemented programs to improve budget transparency at the municipal level and promote the rule of law. In addition, its enforcement of the provisional election rule on incompatibility and conflict of interest has led to the resignation of 136 elected officials from their positions on steering, executive, or supervisory boards of public enterprises and privatization agencies. Seven other officials have resigned from their elected positions. Finally, in late 1999 and early 2000, Transparency International visited Bosnia to meet with international and local personnel involved in combating corruption. Its intent was to establish a Bosnian chapter of Transparency International to develop a local "watchdog" on corruption. As of April 2000, no local chapter had been established.[28]

The United States Has Initiated Several Efforts to Eliminate Corruption

In 1998, USAID conducted a study of corruption in Bosnia and developed an anticorruption strategy.[29] Since that time, the United States has started several anticorruption efforts that address systemic issues such as public accountability and transparency. Two major efforts involve eliminating Bosnian communist-era financial control structures known as payments bureaus and privatizing state-owned enterprises.[30] In addition, U.S. agencies, such as the Treasury Department and the U.S. Customs Service,

[28]In general, local groups contact Transparency International to establish a local chapter. In Bosnia, the Office of the High Representative contacted Transparency International.

[29]USAID has not updated its 1998 anticorruption strategy as it believes the strategy is still relevant and is being implemented.

[30]Yugoslavia developed the payments bureau as a means to maintain complete control over the creation and use of socially owned capital and decision-making in a presumably decentralized system. Unlike most other socialist states, Yugoslavia had a "socially owned" economy where most firms were owned and controlled by the workers and not the state. The five basic functions of the payments bureau are (1) payments, (2) government finance, (3) central bank, (4) private sector bank, and (5) statistics and information. The bureaus are incompatible with a market economy and their activities lack transparency. Until recently, no financial transactions were legal unless conducted through the payments bureau.

assist in taxation reform and conduct training in the control of money laundering. In September 1999, an interagency anticorruption task force led by the State Department was established.[31] This task force functions as an advocacy group for strengthening existing anticorruption mechanisms in Bosnia, such as the Office of the High Representative's Anti-Fraud Unit. As of June 2000, the task force had provided $1 million to the Office of the High Representative's Anti-Fraud Unit to fund auditors, prosecutors, and investigators to work with Bosnian authorities on corruption related cases. The task force was encouraging the international community to provide additional personnel for the Anti-Fraud Unit. As of June 2000 the task force's efforts had not resulted in any measurable reduction in crime or corruption in Bosnia.

One of the major anticorruption activities is the USAID-led effort to reform three separate, political party-based payments bureaus that were established during the 1992-95 war. (Fig. 6 is a picture of the payments bureau in Mostar.) USAID helped to create, and acts as chair of, the multidonor advisory group that is coordinating the reform of the payments bureaus and was responsible for drafting the strategy being used to guide the effort. The reform includes moving the responsibilities of the payments bureaus to other government ministries or banks. For example, tax collection is being moved to the Ministry of Finance, and the payments function is being moved to public and private banks. The ultimate goal of the reform effort is to eliminate the payments bureaus by December 31, 2000.

[31]U.S. agencies and departments participating in the task force include USAID, Treasury, Justice, and Defense, among others.

Figure 6: Croat-Controlled Payments Bureau in Mostar

Source: GAO.

The payments bureaus are being eliminated because they are corrupt and their continued operation is impeding the development of a private banking system, according to USAID in Bosnia. Payments bureau operations lack transparency, and the international community believes that the political parties use income from bureau fees to fund party activities. Currently, all revenue from private and public businesses is sent to the payments bureaus. USAID research on the business and banking community in Bosnia indicates that there are substantive discrepancies in how the bureaus should operate by law and how they actually operate. For example, several respondents surveyed by USAID believed that organized crime leaders had informants within the bureaus who told them which companies had large cash flows. Two of these companies reported that organized criminal elements had demanded percentages of their cash flows that were based on the payments bureaus' financial statements.

The elimination of the bureau in the Republika Srpska appears to be on schedule as some functions have been moved out of the bureau and into appropriate government ministries. In addition, the Federation has passed the internal payments law, which if implemented will remove the payments bureaus' monopoly on payment services. As of March 2000, the Federation had authorized 11 banks to perform certain types of payment transfers. However, no timeline has been established for moving all payment functions to private banks in both entities. Before the bureaus can be eliminated in either entity, a private banking system must be established. According to USAID, experience in Central and Eastern Europe has shown that the best, and possibly the only, way to accelerate the establishment of a sound, competitive commercial banking system that fulfills key market functions is the entry of reputable foreign banks. The U.S. government and international community have been trying to interest a prime-rated international bank to come to Bosnia, with little success.

A second major USAID-led reform effort is the privatization of state-owned enterprises. USAID advisors have played a key role in drafting and facilitating the passage of privatization legislation; establishing key privatization institutions; and conducting training for government officials, enterprise managers, and the media on the privatization process in both entities. USAID is also conducting a privatization education program throughout the entire country to increase public awareness of and confidence in the process. Privatization in Bosnia is viewed as crucial to the economic development of the country, in part because revenues from these state-owned enterprises are used to finance political party activities

and politically and ethnically based organizations that were supposed to be eliminated after the signing of the Dayton Agreement.[32]

The primary form of privatization being used in Bosnia is voucher privatization.[33] When using voucher privatization programs, governments provide citizens with a specific number of vouchers depending on certain criteria such as age or military service. The vouchers can then be sold for cash or used to purchase shares in privatized companies.

Privatization is proceeding slowly, and corruption may undermine the process. According to the United Nations and other experts, the process, which is ultimately determined and implemented by the government, is another opportunity for government and party officials to profit through corrupt activities.[34] For example, officials may solicit bribes from those interested in obtaining certain assets or sell the assets to themselves at prices below their value. The problem is that corruption discredits privatization itself and voucher privatization does not provide the needed capital and business skills to revitalize a country's economy. Most of the companies that are moving into private hands need significant investment capital to modernize. Voucher privatization will not provide this capital because vouchers have been issued to individuals as payment for government debt, thus, the vouchers provide no capital to the enterprise they are used to purchase. European Community, European Stability Initiative, and other officials believe voucher privatization could legitimize political factions' ownership of companies if those factions have

[32]These organizations are referred to as parallel organizations and include procurement organizations and intelligence services among others.

[33]The Office of the High Representative is implementing a separate privatization program in Brcko that will not use vouchers because of the problems associated with voucher privatization. Instead, a consultant is being employed to identify international investors for each of the enterprises to be privatized.

[34]These problems have occurred in other privatization programs in Eastern Europe. See *United Nations Development Program: Corruption and Good Governance, Discussion Paper 3* , United Nations Development Program (New York: July 1997) and Leslie Holmes, *Corruption, Weak States, and Economic Rationalism in Central and Eastern Europe,* Presented at the 9th Annual International Anticorruption Conference (Durban, South Africa: Oct. 1999).

the resources to purchase most of the better companies through private investment funds or other means.[35]

The head of the Office of the High Representative's Economic Department publicly stated in April 2000 that a majority of already privatized companies belong to the nationalist parties. In the Federation, this problem is exacerbated by citizens' sale of vouchers for as little as 3 percent of their face value through newspaper ads. In addition, the documentation required to privatize the companies, including opening balance sheets and privatization plans, is being provided by enterprise managers who are not precluded from bidding on the companies, which is clearly a conflict of interest. According to USAID officials responsible for the privatization effort, no audits of the balance sheets will be conducted. In a USAID survey of businesses in Bosnia, several officials acknowledged depressing the value of their firms so they could purchase them for less than their true value.

The U.S. Ambassador, after several warnings, suspended U.S. funding for the Federation's privatization program in December 1999. He took this action because Federation officials repeatedly missed deadlines for supplying all of the required opening balance sheets and privatization plans needed to allow full-scale privatization to proceed. Consequently, privatization assistance was redirected to Republika Srpska, where privatization is progressing more quickly. The suspension was still in effect as of May 2000. Further, in May 2000, the High Representative removed the president of the management board of the Federation Privatization Agency due to persistent and serious obstruction of the privatization process in the Federation. The board president's actions had led to unsatisfactory results and a lack of transparency in the privatization process.

As an example of how the privatization program can be manipulated, the Sarajevo Holiday Inn (valued at $10 million to $15 million) was purchased for $3 million in March 2000.[36] The U.S. Ambassador to Bosnia has

[35]Any group or organization, including a political party, can establish private investment funds.

[36]The Sarajevo Holiday Inn is a franchise of Bass Hotels and Resorts Incorporated. According to a Bass official, the franchise contract requires the franchise owner to notify Bass prior to the sale of a hotel. No notification was provided to Bass prior to the sale of the Sarajevo Holiday Inn. Failure to notify Bass can result in the termination of the franchise agreement. The government spent $5 million to $7.5 million renovating the hotel after the war.

protested the sale because USAID and the U.S. Embassy believe that the method used to privatize the hotel was inappropriate and not consistent with the privatization program's objectives. The prime minister of the Federation has rebutted these protests by stating publicly that the sale was legal. Government officials allowed the hotel to be classified as a small-scale enterprise, and it could therefore be purchased with vouchers. According to USAID, although the sale of the hotel was publicized in the international press, foreign investors did not have enough information to make an informed decision. The sole bidder, a Bosnian, paid a total of 15 million konvertible marka (5 million in konvertible marka and 10 million in vouchers) for the hotel on March 27, 1999.[37] Since voucher units can be purchased for as little as 3 percent of their value, it is estimated that the local bidder only paid 5 million konvertible marka, or approximately $3 million, for the hotel. As of March 30, 2000, the bidder had provided only the voucher portion of the payment. Figure 7 is a picture of the hotel.

Figure 7: Holiday Inn Sarajevo

Source: GAO.

[37]Konvertible marka is the Bosnian currency which is tied to the German Mark at a one-to-one exchange rate.

Judicial Reform Efforts Seek to Bolster Independence and Professionalism

The international community has implemented a number of efforts to make Bosnia's weak and politically influenced judiciary more independent and professional. In July 1999, the Office of the High Representative developed a comprehensive judicial reform strategy for Bosnia.[38] The strategy focuses on all aspects of the criminal justice system, including initial investigations by the police, prosecutions, and trials. As part of these judicial reform efforts, in July 1999, the Office of the High Representative imposed three laws to expand the jurisdiction of the Federation supreme court, strengthen the Federation prosecutor's office, and provide special witness identity protection. As of May 2000, some steps had been taken to implement these laws, such as the appointment of judges to the Federation supreme court; however, none of the laws had been tested in the courts.

In April 2000, the Republika Srpska government adopted laws on the judiciary and public prosecution. However, due to last minute amendments to these laws, the intent of the laws, that is, the removal of political influence from the judiciary, was not fulfilled. Consequently, the High Representative had to correct the flaws these amendments introduced so that the purpose of the laws could be realized. In the Federation, the High Representative imposed the law on judicial and prosecutorial service due to "intolerable delays" in the legislative process that reflected a lack of will to allow the depoliticization of the judiciary.

The United Nations established the Judicial System Assessment Program in 1998 to monitor and assess the judicial system in Bosnia. The program has created a database on all courts' and prosecutors' offices in Bosnia and has issued judicial sector-related reports with recommendations. Additionally, the U.S. Department of Justice's Office of Overseas Prosecutorial Development, Assistance, and Training, in cooperation with the American Bar Association's Central and Eastern European Law Initiative, has been training judges, prosecutors, and police to understand and implement criminal laws that they helped draft and that were adopted in the Federation.[39] In 1999, the program received U.S. funding to conduct

[38]The judicial reform efforts within the Office of the High Representative are coordinated through an internal Judicial Reform Coordination Group that provides policy guidance on judicial reform issues.

[39]The Federation's criminal code has been reformed. As of March 2000, Republika Srpska's legislature had not passed a reformed criminal code.

training in fighting organized crime, investigating public corruption, and prosecuting those responsible.

Police Reform Is Focused on Training and Democratization of Local Police

The U.N. International Police Task Force has focused its efforts on restructuring, retraining, and democratizing the local police. The task force has established a certification process through which each police officer is evaluated against specific criteria, including involvement in human rights abuses during the war. In addition, the task force has created specialized units to train Bosnian police in public security issues such as organized crime, drug-related activities, corruption, and terrorism. The United States has assisted in police reform in Bosnia through the Justice Department's International Criminal Investigation Training Assistance Program. This program has helped to set up internal affairs units to pursue allegations of police wrongdoing and develop standardized policies and procedures. Police that engage in corrupt or anti-Dayton Agreement activities are removed from office.

The development of a Bosnian state border service has been a priority since December 1997.[40] In November 1999, the presidents of the national government and two entities agreed to support the establishment of such a service. In January 2000, the High Representative imposed a law to establish a single state border service because the Bosnian House of Representatives failed to adopt the law. Initially, the border service is going to be responsible for the Sarajevo airport and 3 of over 400 uncontrolled border entry points in Bosnia.

Although the anticorruption and judicial reform efforts being implemented by the United States and international community are needed, U.S. and international officials said that they have had little success because the political will of Bosnia's leaders is weak or nonexistent. These efforts have not resulted in the successful convictions and jailing of corrupt officials, nor have they curtailed political influence over the judiciary, as discussed previously.

[40]Duties of the state border service will include police surveillance of borders and control of cross-border traffic, including inspection of documents and authorization for crossing the border and apprehension or prevention of illegal entry into Bosnia.

Internal Controls Over International Aid Appear Adequate, but Assistance Supplants Bosnian Funds

The majority of international assistance provided by major donors is in the form of reconstruction projects and technical assistance and is governed by a number of internal controls. International assistance officials believe these controls have protected the majority of international assistance. However, there are no controls on most of the grants and loans provided directly to support the entities' budgets except for those provided by the United States. Further, we identified instances in which corruption has affected the international assistance effort. All of the assistance supplants the monies of the entity governments; consequently, it frees up government funds for uses over which the international community has no control. Finally, while the international community provides assistance and funds, the entity governments are losing hundreds of millions of dollars in public revenues due to corruption, an irrational tax system, and widespread customs duty and tax evasion, according to USAID, the Office of the High Representative, the Customs Assistance Office, and the International Crisis Group.

Controls on International Assistance

The unanimous opinion of the international officials we spoke to, including the U.S. Ambassador, the Deputy High Representative, and European Commission officials, is that the controls on international project assistance are adequate and that there is no evidence that assistance is being lost to large-scale fraud or corruption in Bosnia. The audit reports made available to us did not indicate that large scale losses had occurred. The nearly $4 billion in assistance provided from January 1996 through December 1999 by major donors such as the World Bank, the European Commission, the European Bank for Reconstruction and Development, and the United States includes reconstruction projects, technical assistance, or business development loans. The assistance is delivered and managed by international contractors or the assistance agencies themselves and is subjected to on-site monitoring and periodic audits.

Monitoring of each World Bank project is done twice a year, according to Bank officials. In addition, Price Waterhouse annually audits all 20 of the World Bank's projects that are financed with International Development Association funds.[41] The results of the audits are provided to both the

[41]The International Development Association is the World Bank's concessional lending organization. It provides long-term loans at zero interest to the poorest of the developing countries.

World Bank and the Bosnian government. The audits are primarily financial audits; however, compliance with conditions in the loan agreements is also examined. In addition to the annual audits, reports on completed projects are prepared and provided to the World Bank and the Bosnian government. These reports examine the impact of the projects. The World Bank conducts further reviews of the projects based on a sample of the reports.[42]

The European Bank for Reconstruction and Development provides assistance exclusively in the form of loans to the government of Bosnia for business development projects. Although the loans are made to the government, it never actually controls the money. Instead, the bank pays the suppliers of goods and services on the various projects directly. In addition, all of the bank's programs are regularly audited by one of the large international audit firms.

To ensure that USAID's program funding is accounted for and used appropriately, USAID's Office of the Inspector General has conducted concurrent audits and investigations of the agency's two major assistance efforts in Bosnia, the Municipal Infrastructure and Services Program and the Business Development Program.[43] These audits have been conducted since the programs started in 1996. No major systemic internal control weaknesses or misuse of program funds were identified in the first project; however, the following significant problems were found in the Business Development Program:

- repeated instances of program abuses and misuse of funds by participating banks and borrowers in the program,
- inadequate monitoring of participating banks and borrowers, and
- a delinquency rate representing at least 50 percent of the loans.

[42]A previous GAO audit concluded that the Bank's effort to improve management controls "entailed making major improvements in the Bank's internal oversight structure, project management, and institutional development strategies. However, these controls, although improving, are not strong enough to provide reasonable assurances that project funds are spent according to the Bank's guidelines. Significant weaknesses still exist in each of the key components of the Bank's management control system." (*World Bank: Management Controls Stronger, but Challenges in Fighting Corruption Remain* (GAO/NSIAD-00-73, April 6, 2000).

[43]The Municipal Infrastructure and Services Program is an initiative to rehabilitate basic infrastructure to facilitate the return of refugees to their homes and reactivate the local economy. The Business Development Program provides loans to Bosnian enterprises on concessionary terms in an effort to rebuild the economy.

USAID has taken corrective actions in response to the problems identified by the audits and investigations. Monitoring efforts have been strengthened, and the delinquency rate has decreased. Further, litigation and foreclosure actions are being pursued, and investigations have resulted in the termination of a foreign service national employee who used their position for personal gain.

Some Corruption and Fraud Have Occurred in the International Assistance Effort

We were told of instances in which fraud and corruption occurred within the international assistance effort. Specifically, the United States, the Organization for Security and Cooperation in Europe, other donors, and Bosnian citizens have been unable to recover funds from BH Banka, a Bosnian bank involved in illegal activity, according to the U.S. Ambassador to Bosnia. The United States had about $934,000 in the bank, approximately $384,000 in embassy operating funds and about $550,000 in USAID money that was being repaid on successful business loans but was not transferred by BH Banka to Bank America as required. The Federation Banking Agency has taken steps to rectify the situation, including closing the bank and liquidating its assets. The Federation government offered to pay the United States the approximately $1 million directly, ahead of all other creditors. The United States refused this offer because it wants the matter dealt with openly, transparently, and in accordance with international business practices, so that all depositors will be repaid. According to the State Department, the Federation Banking Administration is conducting audits as part of a plan to keep pressure on the bank's owners to repay all of the bank's depositors. The U.S. Embassy, Sarajevo, has brought pressure on Federation authorities to prosecute the bank's corrupt owners and force them to repay their creditors. However, as of June 2000 the funds had not been returned to depositors, including the United States.

In addition to the BH Banka case, three other banks have been terminated from the Business Development Program for repeated serious violations of their responsibilities under the program's guidelines. For example, in several cases the banks did not disclose the status of their own existing loans to prospective borrowers and credited the payment on program loans to their own loans with the borrowers. In one case, a borrower claims to have been blackmailed into taking out a short-term bank loan with a bank in order to receive a Business Development Program loan. Criminal cases are being aggressively pursued against these banks by USAID. For example, in one case, the criminal court issued a 54-page verdict that convicted a number of bank officials. Three bank officials and two cashiers received jail sentences ranging from 6 months to 4 years and 3 months. The

bank is in liquidation, and over $620,000 in undisbursed loans remain at risk. Criminal investigations are ongoing in the other two banks.

Further, in July of 1998, the contract of a USAID foreign service national serving as the program manager for the Business Development Program was terminated for inappropriate conduct. In this case, a potential borrower seeking a Business Development Program loan contacted the program manager for assistance. The potential borrower paid the program manager for the assistance. When the program manager requested additional funds, the potential borrower contacted USAID in Sarajevo and reported that a USAID employee had promised to help his company but at a price. The ensuing investigation resulted in the termination of the program manager's contract.

The World Bank has also been affected by corruption in Bosnia. In 1997, approximately $340,000 in World Bank-provided funds were lost as a result of a Bosnian procurement scheme perpetrated with fraudulent procurement authorization documents. As of May 2000, no arrests had been made and no funds had been recovered.

Finally, an American citizen employed as the Deputy Commissioner of the U.N. International Police Task Force in Bosnia was removed in the summer of 1999 because of his involvement in corrupt activities.[44] According to the U.N. mission in Bosnia, Bosnian Croat government officials were providing the deputy commissioner with in-kind payments, including an apartment and a car. Although removed from office and returned to the United States, as of June 2000, neither the United Nations nor the U.S. government had brought any further charges against the former deputy commissioner or conducted an investigation to determine whether the Deputy Commissioner had used his position to benefit the entity ministries of the interior. In commenting on a draft of this report, the State Department indicated that the case is now being referred to its Office of the Inspector General.

Budget Support Assistance Frees Money for Other Uses

The World Bank, the International Monetary Fund, the European Union, the U.S. government, and others have committed over $407 million in direct

[44]The U.S. Department of State provides Americans serving in the U.N. International Police Task Force through a contract with a private company. The officers' salaries are paid by the State Department contractor; their per diem is paid by the United Nations.

support to the entities' budgets. This budgetary support was provided for agreed-upon entity budgets and included conditions on strengthening public financial management and transparency in public spending.[45] Table 1 lists the amounts of budgetary support committed by the international community.

Table 1: Budget Support Committed by the International Community for the Federation and Republika Srpska

Organization	Amount
World Bank[a]	$244.5
International Monetary Fund	70.0
European Union	60.0
United States[b]	27.0
Other	5.9
Total[c]	**$407.4**

[a]World Bank funding includes trust funds financed by other donors.

[b]Includes $22 million committed to Republika Srpska and $5 million committed to the Federation but not disbursed due to the Federation government's lack of compliance with U.S. conditions placed on the funding. The United States has tried to persuade other donors to place conditions on the budget support they provide.

[c]Total does not include all budget support provided by all international donors because information on all donors is not readily available. Total does not include cash transfers from Serbia or Croatia. Estimates of these transfers total more than $500 million from 1996 through1999.

Source: World Bank, International Monetary Fund, European Union, USAID, Office of the High Representative, and International Management Group.

As reconstruction project-related assistance has been reduced, budget support is accounting for a larger percentage of total assistance. For example, the Republika Srpska Aid Coordination and Development Unit estimated that budget support accounted for approximately 20 percent of total assistance being provided as of December 30, 1999. The World Bank plans to provide an additional $150 million in budget support to Bosnia over the next 2 to 3 years. The World Bank's budget support is conditioned on the entity government's implementing certain budgetary reforms designed to improve accountability and transparency.

[45]Appendix II provides information on entity revenues and budgets.

Despite running budget deficits, the Federation and Republika Srpska spent approximately 41 and 20 percent, respectively, of their average annual, domestically financed revenue on military expenditures from 1997 through 2000, according to budget documents they submitted to the International Monetary Fund.[46] This percentage does not include military funding provided by other nations, most notably from Serbia to the Republika Srpska and from Croatia to the Bosnian Croat military in the Federation.[47] International Monetary Fund, World Bank, and European Commission officials told us that the funding provided by their organizations is not audited, primarily due to its fungibility, and that support funding does free up domestic revenues that can be used by the entity governments for any section of their budgets. According to the Director of the Republika Srpska Aid Coordination and Development Unit, the international community attaches little consideration to how the money is spent. Further, because of the lack of transparency in entity budgets and the fungibility of money, it may be impossible to determine how the money was used. According to the World Bank, no audits of the entities' expenditures have been conducted. The Office of the High Representative's comptroller told us that due to the lack of adequate bookkeeping in Bosnia, no major accounting firm would do an audit of Bosnian government accounts and come up with a firm audit opinion on which they would stake their reputation.[48]

In 1998 and 1999 the United States provided $22 million directly to the Republika Srpska budget to pay the salaries of teachers, doctors, and staff of the Ministry of Refugees. According to the Department of State, the budget support provided to Republika Srpska, among other things, "bolstered a moderate government and helped prevent Belgrade-supported parties from deterring Dayton implementation." The Office of the High Representative administered the U.S. budget support funds. USAID, in

[46]In an address to the North Atlantic Council in May 2000, the High Representative stated that "a stable security environment in Bosnia will not be possible so long as three, relatively large, separate armies exist in Bosnia which are primarily designed to fight each other … the current size and structure of the Entity Armed Forces are at gross variance with the defense needs of Bosnia and are not financially sustainable."

[47]According to the Organization for Security and Cooperation in Europe, in 1999 the Croatian Ministry of Defense provided the Bosnian Croat army $71 million that was used for undisclosed operational costs. On March 8, 2000, after a change in the Croatian government, Croatia signed an agreement under which all requests for and approvals of security assistance to Bosnia will be made transparent.

[48]In April 2000, the Parliamentary Assembly appointed auditors for Bosnia.

conjunction with the Office of the High Representative, designed the internal controls for the distribution of this money. The High Representative's comptrollers office audited the program twice using a statistical sampling methodology. USAID's Inspector General's Office participated in the audits and reviewed Office of the High Representative's audit reports. USAID's Inspector General audit reports on the program indicate that the support funds were used for their intended purpose and no major problems occurred in the program. The High Representatives comptroller's office stated that no other program in Bosnia has as rigorous a follow-up program or audit program as the USAID support program.

Customs and Tax Evasion Are Believed to Result in the Loss of Hundreds of Millions of Dollars in Revenue

Widespread customs duty and tax evasion result in massive revenue losses. Determining the total amount of revenue lost would be difficult, and the international community has not systematically attempted to quantify these losses. However, evidence gathered during successful customs investigations and partial analysis by the Office of the High Representative suggest that the losses total hundreds of millions of dollars annually. For example, two investigations conducted by the Customs Assistance Office in 1997 found that $22 million in customs and tax revenues were lost over the period of 1 year. A later investigation conducted by the Republika Srpska customs administration in 1998 identified illegal activity that resulted in the loss of $29 million in revenue. In still another investigation involving customs administrations in both entities, revenue losses were estimated at over $78 million.

The overall loss of revenue from the underground economy—including the loss of sales, business, and income taxes—is far greater than the losses resulting from customs duty evasion according to the Customs Assistance Office. For example, according to USAID and International Crisis Group reports, an irrational tax system forces business to evade taxes in order to operate; consequently, government revenue is lost. For example, tax and benefit contributions amount to 87 percent of a worker's salary. The amount is not deducted from a worker's salary but instead is paid to the state in addition to the salary. In addition, a warm meal tax of $42 must also be paid monthly. Consequently, if an employee is paid $100 a month, the employer must pay the state an additional $129 per month. According to surveys of the business community by USAID and the International Crisis Group, such irrational taxes are almost always evaded. Businesses avoid these taxes by paying their employees in cash and do not report to the government information on the people they hire.

The Office of the High Representative has publicly stated that the entity governments lose hundreds of millions of dollars in revenues to corruption and fraud every year. In its 1999 analysis of customs and tax evasion in Republika Srpska, the Office of the High Representative concluded that a moderate estimate of all tax evasion is $136 million annually, which means that Republika Srpska's budget would be essentially in balance without foreign support if it had a rational tax system and collected the revenues that it is currently losing. The Director of Republika Srpska Aid Coordination and Development Unit echoed this view.

The international community continues to provide funds directly to the entities' budgets despite repeated guidance that assistance should not be substituting for diverted or lost revenue. Specifically, in December 1997, the Peace Implementation Council stated that

> "Foreign aid must not be a substitute for diverted state resources. Donors have to protect their assistance funds from possible misuse, as well as having to compensate for misappropriation. The Council recognizes that the lack of transparency and accountability of public finances… undermines democratic values and the prospects for foreign investment in both entities."

In its March 1998 proposal for systemic reforms pertaining to fraud and corruption, USAID stated that

> "the losses resulting from fraud and corruption appear massive, yet cannot be quantified accurately due to the lack of transparency in government and business operations. [The diverted funds from public companies and other public funds may be financing political party activities and the continued existence of illegal parallel institutions.] This directly threatens the new government's legitimacy, perpetuates ethnic divisions, and is hostile to the rule of law."

And in a June 1999 presentation on corruption, the U.S. ambassador then in Bosnia stated that the international community was concerned about corruption because the provision of U.S. assistance frees money for corrupt uses, which in turn endangers the implementation of the Dayton Agreement, that is, the establishment of a democratic society based on the rule of law.

Conclusions

The United States and other international donors have committed more than $4 billion since January 1996 to finance the international reconstruction and recovery program designed to implement the civilian aspects of the Dayton Peace Agreement. Most of this funding supported

Bosnia's physical reconstruction, which has largely been successfully completed. The international efforts also include programs to fight corruption, promote democratic government based on the rule of law, and facilitate a free-market economy—all of which constitute important building blocks toward reform. Senior U.S. and international officials in the region have concluded that this assistance has not resulted in self-sustaining reforms.

U.S. and international officials believe the benchmarks for implementing the Dayton Agreement cannot be met because Bosnian leaders have not demonstrated a commitment to combat corruption and remove political influence from the judicial system and the economy. Consequently, the international community, through the High Representative, has been forced to dictate reforms. Federation officials' lack of cooperation with the U.S. assistance program to privatize state-run enterprises culminated in the U.S. Ambassador's December 1999 decision to suspend U.S. funding for such efforts, an example of U.S. officials' growing frustration. Although a few government organizations and officials have investigated corruption in Bosnia, they have acted against political and economic vested interests at risk to their own personal safety and that of their families. In the absence of Bosnian leaders commitment to address crime and corruption, Bosnian law enforcement and judicial systems continue to be subject to corruption and influence, and efforts to rebuild the economy have been stymied.

Bosnian leaders may have little incentive to combat corruption and tax evasion, since reducing corruption may reduce their ability to maintain their power and authoritarian control over the country. However, if customs and tax evasion were reduced and accountability improved, government revenues would increase; this increase would reduce the need for external budget support from international donors.

U.S. and international donors are now faced with a dilemma. On one hand, after 5 years of donor funding for civilian reform programs, Bosnian political leaders have not demonstrated a commitment to reform and in fact continue to block well-intentioned reform efforts. On the other hand, some fundamental structural initiatives, such as eliminating payments bureaus, need to go forward with associated financial support. Without the benefit of a fundamental reassessment of the strategy for providing assistance and achieving the goals of the Dayton Agreement, the United States and other donors may continue to expend funds on initiatives that have little hope of resulting in a self-sustaining democratic government and

market economy based on the rule of law, thus creating the conditions that could lead to the complete withdrawal of NATO-led forces.

Recommendations

We recommend that the Secretary of State take the lead in conducting a reassessment of the U.S. strategy for assisting Bosnia to achieve the objective of establishing a democratic government and a market economy. We recommend that the Department of State:

- evaluate unilateral and multilateral options for modifying the type and amount of assistance provided (including a review of the appropriateness of providing general budget support), place strict conditions on future assistance, and possibly suspend assistance until Bosnian political leaders independently demonstrate their determination to fight organized crime and corruption;
- consider whether direct budgetary support is an appropriate form of assistance in the current environment in Bosnia; and
- determine how it can support those political leaders in Bosnia whose goals for addressing the problem of crime and corruption are consistent with the goals of the U.S. and the international community.

Matters for Congressional Consideration

Congress may wish to consider conditioning future U.S. assistance to Bosnia on an explicit requirement that the State Department certify that the Bosnian governments have taken concrete and measurable steps to implement anticorruption efforts and significantly improve their ability to control smuggling and tax evasion.

Agency Comments and Our Evaluation

The Departments of State and Defense and the U.S. Agency for International Development provided written comments on a draft of this report. (These comments are reprinted in their entirety in apps. IV, V, and VI, respectively) The Department of Defense agreed with our assessment that crime and corruption are endemic in Bosnia and are impeding the economic, political, and judicial reform aspects of the Dayton Peace Agreement. USAID did not disagree with our findings, conclusions, or recommendations, and stated that it is now reassessing its country strategy. It said that the information contained in our report will be considered in its development, but it cautioned against the use of broad based conditions such as suspending U.S. government assistance until the conditions are

met. We do not specifically suggest the use of such conditions but rather we suggest that all options be reassessed given the current situation.

The Department of State did not disagree that crime and corruption impede the success of the Dayton Peace Agreement, and it specifically agreed that direct budget support should be carefully evaluated because of the difficulty in establishing firm controls over its use. However, State disagreed with our report's characterization that Bosnian leaders have not demonstrated the political will to combat crime and corruption. State acknowledged that while certain government officials oppose reform, some moderate officials have cooperated and others have cooperated under pressure. State pointed to several laws that have been adopted as a sign of success.

State disagreed with our recommendation that its assistance strategy be reassessed. According to State, by 1998, it had undertaken a broad reassessment of its assistance, and that it continually reassesses assistance priorities towards Bosnia. State's comments outlined a series of program and funding adjustments made as a result of its reassessment. We recognize that State assesses assistance levels for various program categories on an ongoing basis; and we support such periodic reassessments. However, we found no evidence that State's reassessment process addressed the underlying causes of corruption and a lack of reform, namely the continued obstructionist behavior of the hard-line nationalist political leaders and others who State acknowledged have obstructed reform efforts promoted by the international community. As indicated in State's comments, there are moderate political leaders in Bosnia with whom it can work. Reassessing the assistance strategy, taking into account root causes, is important because crime, corruption, and political influence over the judiciary, government operations, and the economy continues to be endemic. Despite State's 1998 reassessment, Bosnian leaders still have not taken ownership of the reform efforts encouraged by the international community, nor have they independently demonstrated that they are willing to take action to curb crime and corruption and develop and support a functioning judiciary.

We believe that while State's reassessments of program priorities are important, such assessments have been limited and have not fully examined the root causes of the endemic crime and corruption in Bosnia nor have they considered what adjustments in assistance strategy would address these root causes. Adjusting the level of U.S. support for business lending or budget support as cited by State, for example, while important on their own merits, does not address the linkage that exits between

Bosnia's political leaders and the corrupt entities controlled by the political parties. It is matters such as these that we believe should be examined as part of a comprehensive reassessment of the assistance strategy for Bosnia.

We are providing copies of this report to the Honorable Madeleine K. Albright, the Secretary of State; the Honorable William S. Cohen, the Secretary of Defense; the Honorable J. Brady Anderson, Administrator for the Agency for International Development; and interested congressional committees. Copies will be made available to other interested parties upon request.

If you or your staff have any questions about this report, please contact me at (202) 512-4128. An additional GAO contact and staff acknowledgements are listed in appendix VIII.

Harold J. Johnson, Associate Director
International Relations and Trade Issues

Benchmarks for Measuring Progress in Implementation of the Dayton Peace Agreement

The General Framework Agreement for Peace in Bosnia and Herzegovina, more commonly known as the Dayton Peace Agreement, was initialed in Dayton, Ohio, on November 21, 1995. The agreement contains 11 articles endorsed by the parties to the peace settlement and 11 annexes containing details for implementation. Representatives from Bosnia, Croatia, and the Federal Republic of Yugoslavia signed the agreement in Paris on December 14, 1995. Table 2 lists the annexes and ties them to 10 benchmarks that the U.S. executive branch believes must be achieved if the Dayton Agreement is to succeed. The Dayton Peace Implementation Council and the North Atlantic Council have adopted similar benchmarks for evaluating the implementation of the Dayton Peace Agreement.

Table 2: U.S. Executive Branch Benchmarks for Measuring Progress in the Implementation of the Dayton Peace Agreement

Annex	Benchmark
Annex 1-A: Agreement on the Military Aspects of the Peace Settlement calls for a cease-fire, withdrawal of foreign forces, redeployment of national forces, and deployment of an international Implementation Force.[a] In addition to ensuring compliance with the agreement and maintaining a secure environment, the Implementation Force assists international agencies in the provision of humanitarian and development assistance. **Annex 1-B: Agreement on Regional Stabilization** deals with regional and subregional arms control.	**Military stability:** Continued cease-fire. **Persons indicted for war crimes**: Cooperation with the International Criminal Tribunal for the former Yugoslavia, leading to the transfer of indicted war criminals to The Hague for trial.
Annex 2: Agreement on Inter-Entity Boundary Line and Related Issues establishes the interentity boundary line and the arbitration for the Brcko area.	**Brcko**: Implementation of the Brcko Arbitration Tribunal's Final Award that was issued on March 5, 1999.
Annex 3: Agreement on Elections lays the foundation for democratic elections, establishes a permanent election commission, and requests that the Organization for Security and Cooperation in Europe supervise and monitor elections.	**Elections and democratic governance:** Establishment of national democratic institutions and practices. **Media reform:** Establishment of a regulated, independent, and democratic media.
Annex 4: Constitution of Bosnia and Herzegovina sets the responsibilities of the entities and the institutions in Bosnia and the national government structure.	**Illegal institutions, organized crime, and corruption:** Dissolution of illegal pre-Dayton Agreement institutions.
Annex 5: Agreement on Arbitration requires the entities to design and implement a system of arbitration to resolve disputes between them.	
Annex 6: Agreement on Human Rights describes the fundamental rights and freedoms of Bosnian citizens and establishes the Commission on Human Rights, the Human Rights Ombudsman, and the Human Rights Chamber.	

Annex	Benchmark
Annex 7: Agreement on Refugees and Displaced Persons defines the rights of refugees and displaced persons, states that suitable conditions for return must be created and local leaders must cooperate with international organizations, and establishes a Commission for Displaced Persons and Refugees.	**Displaced person and refugee returns:** Establishment of a functioning, phased, and orderly minority return process.
Annex 8: Agreement on Commissions to Preserve National Monuments establishes the Commission to Preserve National Monuments.	
Annex 9: Agreement on Establishment of Bosnia and Herzegovina Public Corporations establishes the Commission on Public Corporations.	**Economic development:** Implementation of free-market reforms.
Annex 10: Agreement on Civilian Implementation of the peace settlement sets up the Office of the High Representative.	
Annex 11: Agreement on International Police Task Force establishes the international police assistance program to, among other things, monitor, observe, and advise on law enforcement matters, including judicial activities.[b]	**Public security and law enforcement:** The restructuring and democratization of the police force in both entities. **Judicial reform:** Establishment of an effective judicial reform program.

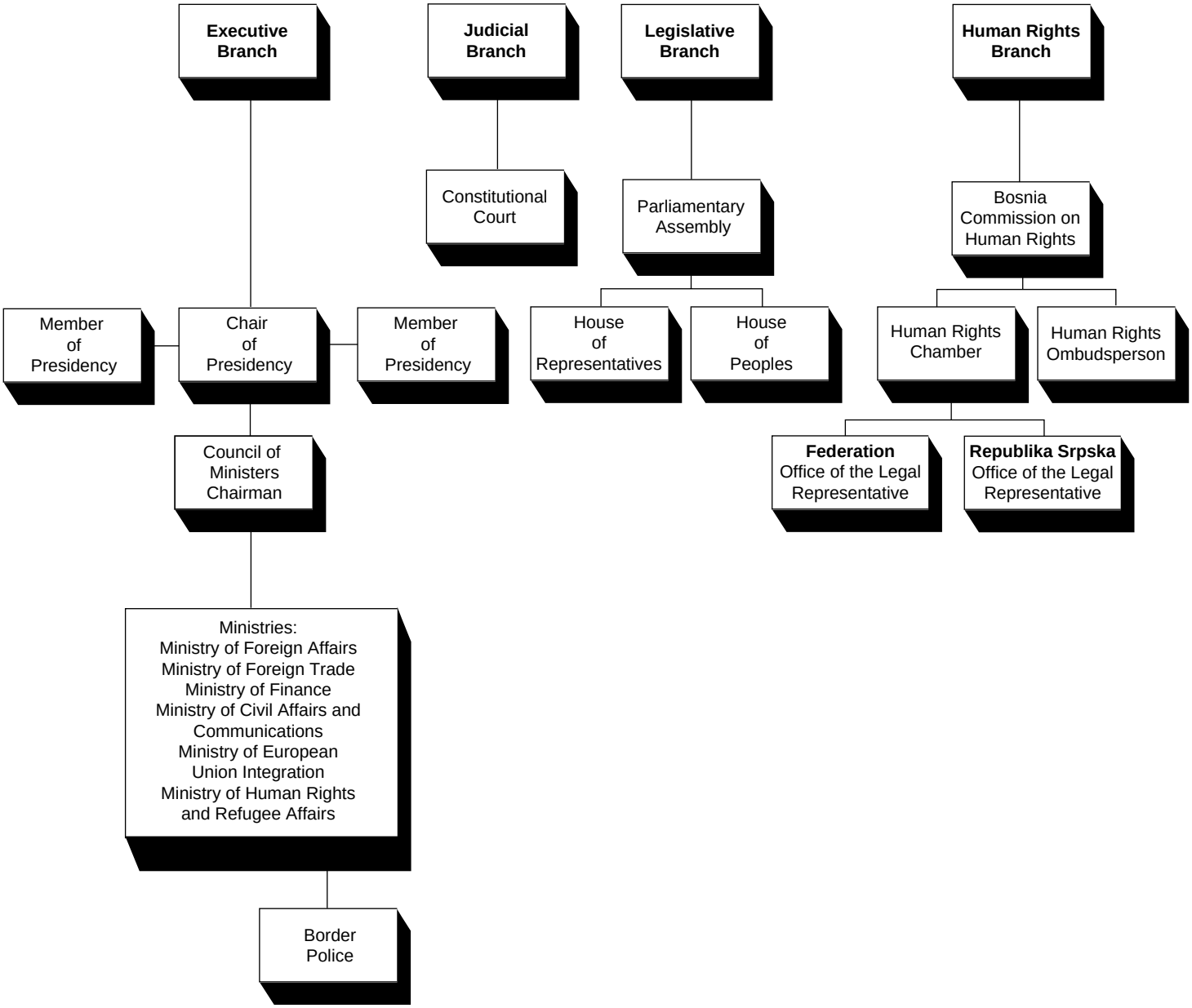
[a]The Implementation Force was the predecessor of the NATO-led Stabilization Force that is currently responsible for implementing Annex 1-A.

[b]Under the Dayton Agreement, the United Nations International Police Task Force oversees judicial activities. In 1998, the U.N. Security Council adopted resolution 1184, which established the U.N. Judicial Assessment Program to monitor and assess the court system in Bosnia.

Bosnian Government and Judicial System Organization and Budgets

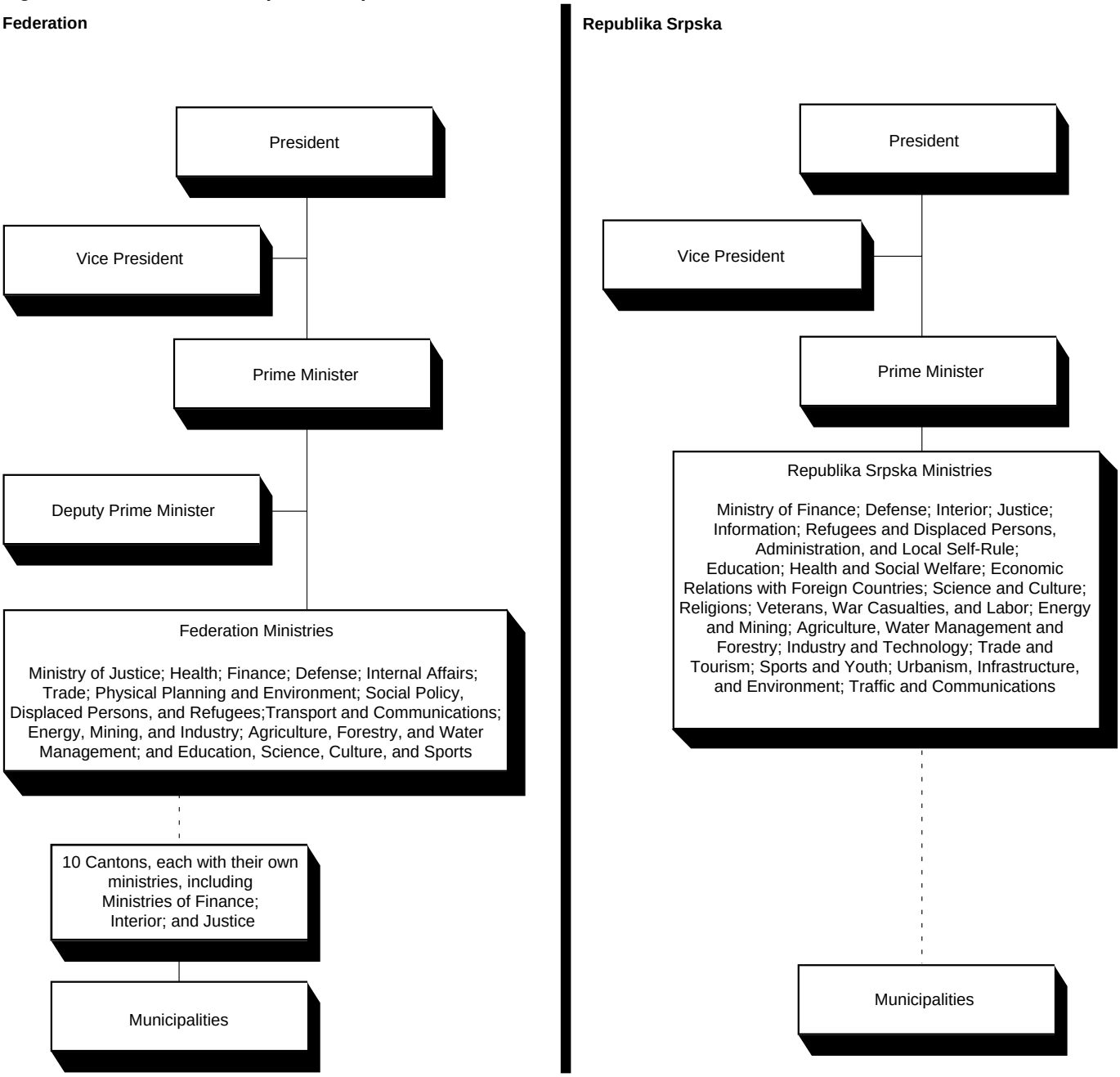
Figures 8-11 show the organization of the Bosnian governments and judicial systems. Figure 12 shows where the two entity governments, the Federation and Republika Srpska, generate revenues. Table 3 describes the entities' budgets.

Figure 8: Bosnia's National Government Structure



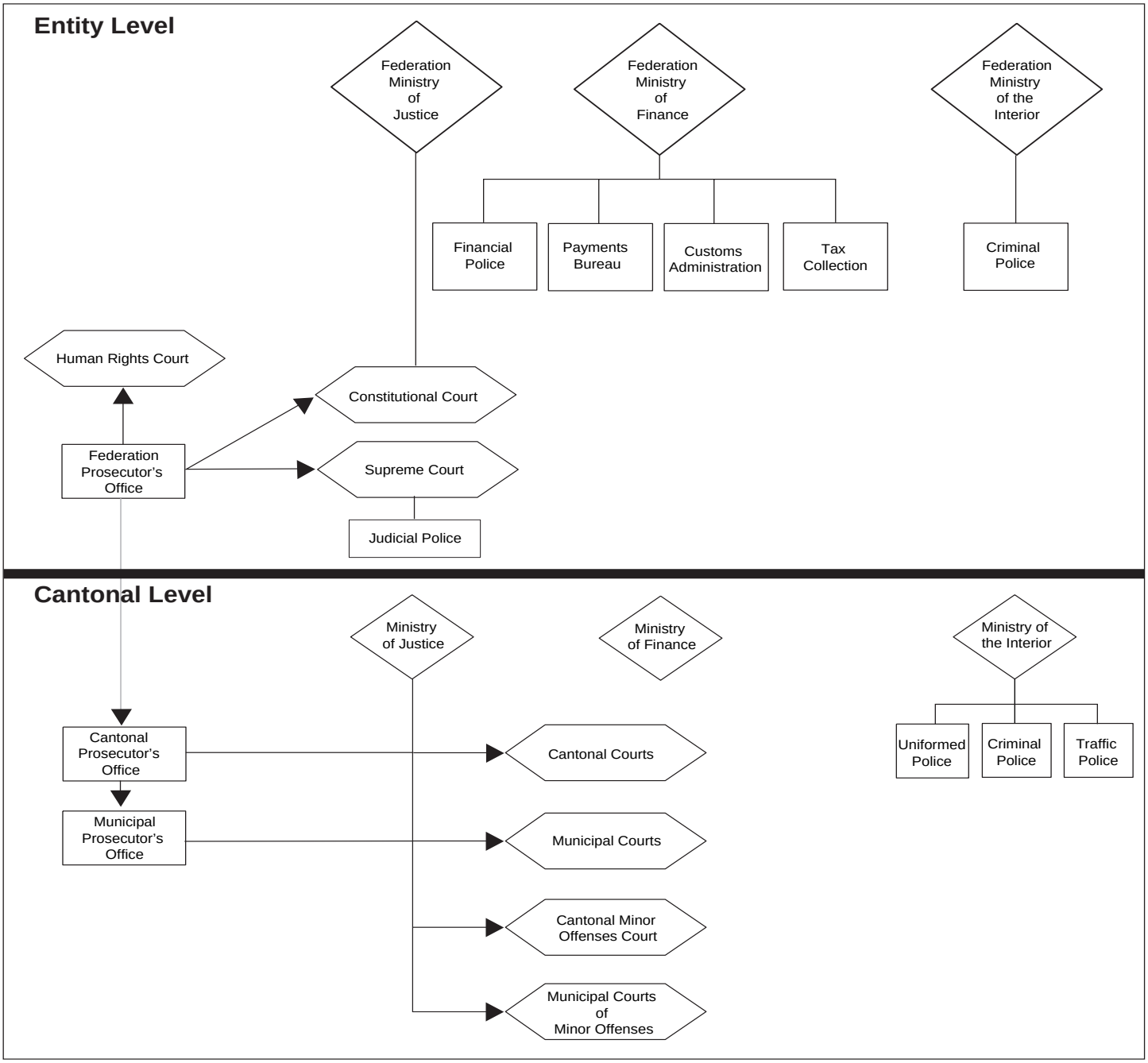
Source: The U.S. Embassy, Sarajevo.

Figure 9: Federation and Republika Srpska Entities' Government Structures



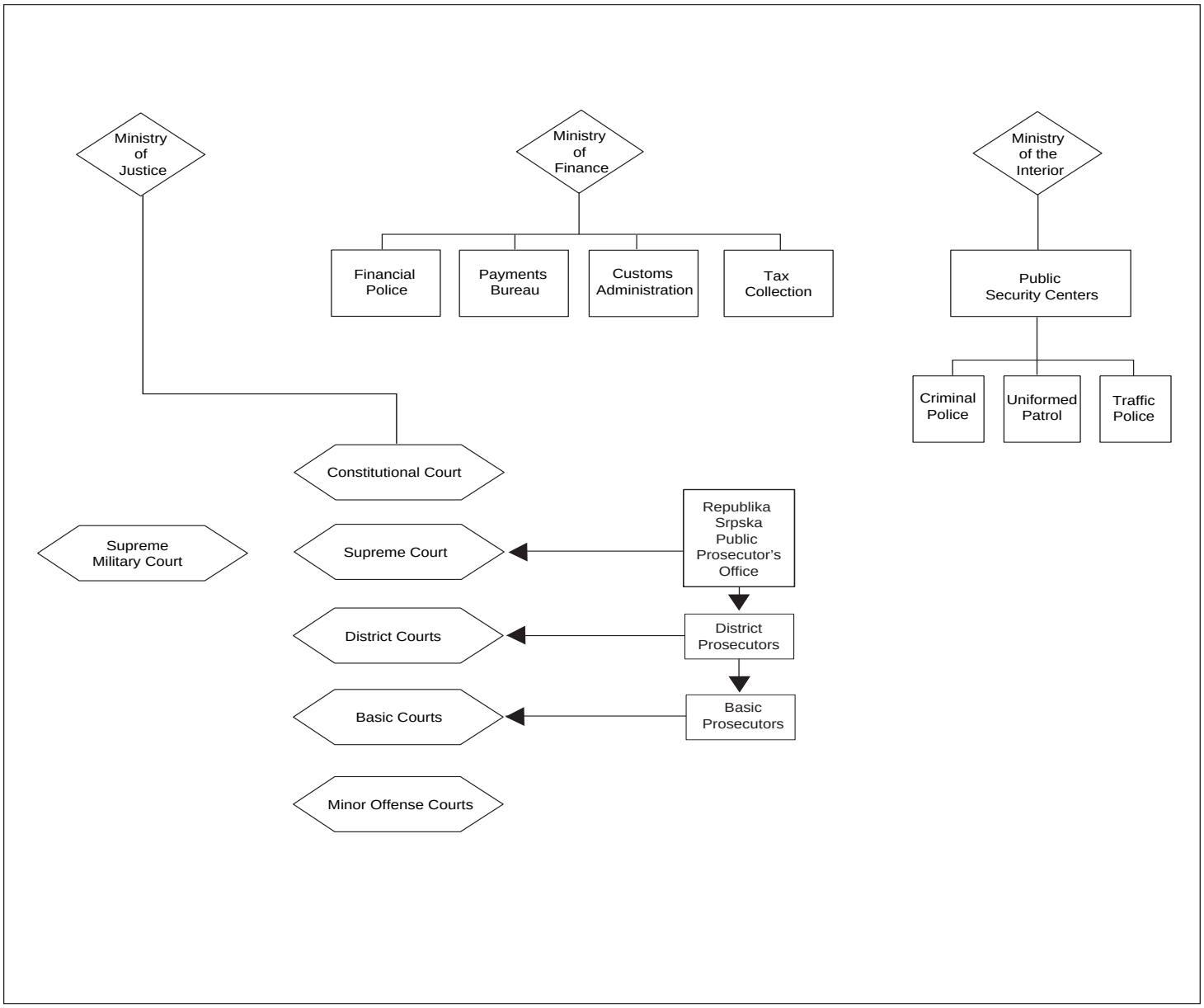
Source: The U.S. Embassy, Sarajevo

Figure 10: Federation Entity and Cantonal Law Enforcement and Judicial Systems



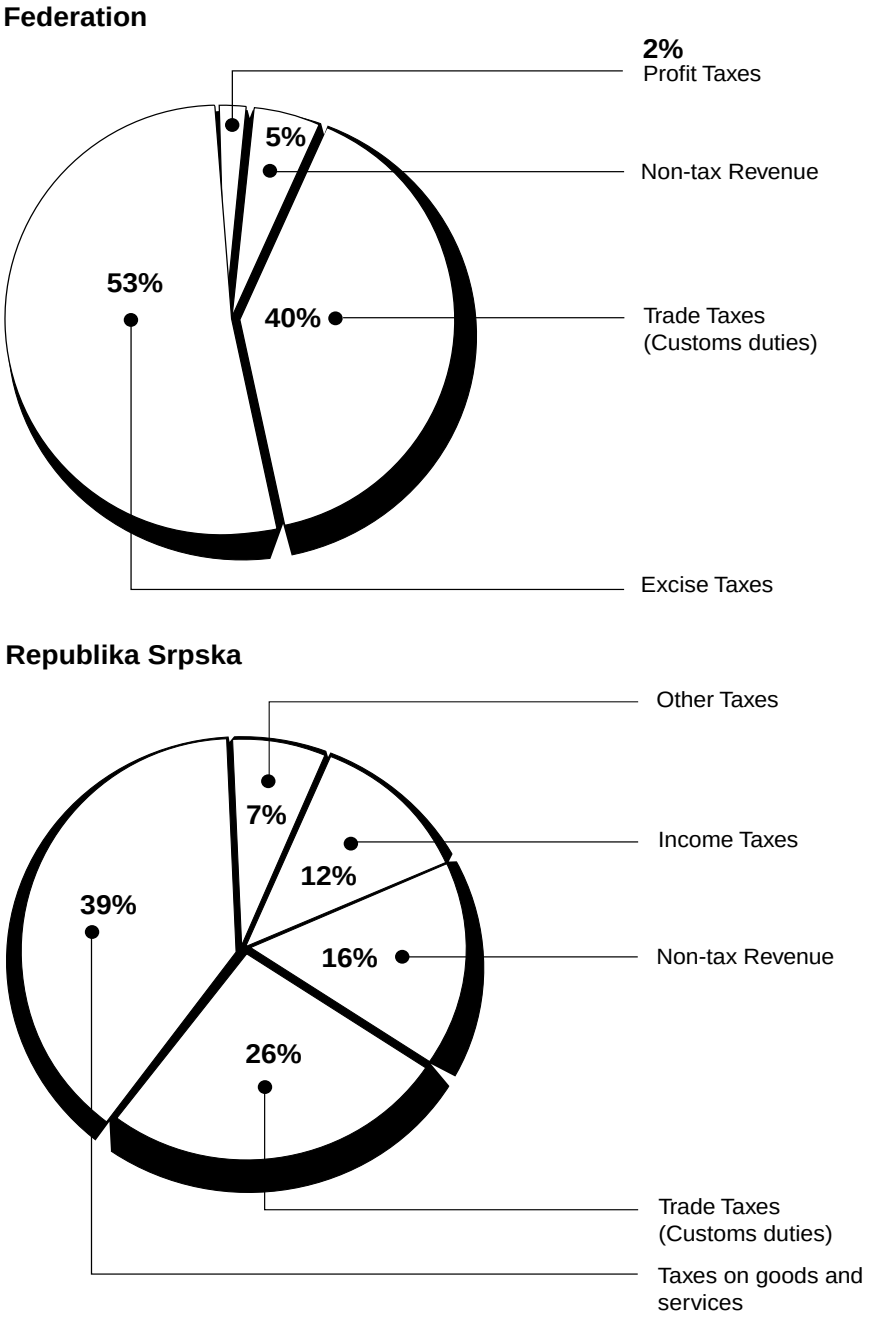
Source: The U.S. Embassy, Sarajevo, and the U.N. Judicial System Assessment Program.

Figure 11: Republika Srpska Entity Law Enforcement and Judicial System



Source: The U.S. Embassy, Sarajevo, and the U.N. Judicial System Assessment Program.

Figure 12: Revenue Sources in the Federation and Republika Srpska (1999)



Source: International Monetary Fund.

Table 3: 1999 Budgets for the Federation and Republika Srpska (average exchange rate for konvertible marka in 1999 was $1=1.836km)

Dollars in millions		
Federation Fiscal Operations 1999		**Percentage of total**
Excise tax revenue	$236.4	52.9
Trade taxes	179.7	40.2
Profit tax	7.1	1.6
Non-tax revenue	23.4	5.2
Total Revenue	**$446.6**	
Wages and contributions	$45.4	9.1
Goods and services	17.6	3.5
Military	200.4	40.0
Reconstruction expenditure	11.5	2.3
Subsidies	7.6	1.5
Transfers to war invalids	147.6	29.5
Other transfers to households	6.6	1.3
Transfers to the state government	47.9	9.6
Transfers to cantons and municipalities	1.4	0.3
Other expenditure and unallocated	14.9	3.0
Total expenditures	**$500.9**	
Budget deficit	**$54.3**	
Foreign loans and grants for budget support	**$54.3**	
Republika Srpska fiscal operations 1999		
Taxes on goods and services	$120.4	38.7
Trade taxes	82.4	26.4
Taxes on income	37.3	12.0
Other taxes	21.5	6.9
Non-tax revenue	49.9	16.0
Total revenue	**$311.5**	
Wages and contributions	$102.3	29.5
Goods and services	66.3	19.1

(Continued From Previous Page)

Republika Srpska fiscal operations 1999		
Military	46.4	13.4
Reconstruction expenditure	21.1	6.1
Banking fees	0.4	0.1
Transfers to social funds	16.5	4.8
Subsidies	6.0	1.7
Transfers to war invalids	30.5	8.8
Other transfers to households	8.1	2.3
Transfers to the state government	32.7	9.4
Transfers to municipalities	0.7	0.2
Other expenditure and unallocated	15.9	4.6
Total expenditures	**$346.9**	
Budget deficit	**$35.4**	
Foreign loans and grants for budget support	**$35.4**	

Source: International Monetary Fund.

Bosnian, International, and U.S. Anticorruption Efforts

The Bosnians and the international community have implemented a wide range of anticorruption and judicial reform efforts. Although necessary, these efforts have done little to reduce crime and corruption or political influence and control of the judicial and law enforcement systems in Bosnia. Further, as of April 2000, the Office of the High Representative stated that none of the achievements are self-sustaining.

Table 4: Major Bosnian, International, and U.S. Anticorruption and Judicial Reform Efforts

Implementor	Date established/activity	Comments
Bosnian efforts		
Entity governments	Ongoing: Modernization of laws	The fundamental basis for fighting corruption is the modernization of laws. An example is the passage of the criminal code in the Federation. This code provides law enforcement officials the foundation for prosecuting government officials and others for corruption charges. The criminal code in the Republika Srpska is currently pending approval in parliament.
Entity governments	Ongoing: Implementation of anticorruption legislation	The federation has adopted legislation, such as the special witness identity protection in criminal proceedings, the law on judicial selection process, and the Bosnia customs laws. The Federation is also adopting the law on auditing the budget, under which an audit office would be established to review the disbursements, expenditures, financial reports, and transactions of the Federation.
Entity governments	Ongoing: Financial police	Under the Ministry of Finance in the Federation. The responsibilities of the financial police include investigations of tax and customs evasion.
Entity governments	Ongoing: Judicial police	The judicial police were established in the Federation in 1996 and are being established in the Republika Srpska. This is a mechanism to ensure the functioning and security of court proceedings, including securing information, witnesses, and accused persons. As of July 1999, the police were operational in 2 out of 10 cantons in the Federation.
Federation government—Chairman of Bosnia presidency	1997-98: Corruption Commission	The Commission never became operational.
Federation government—House of Representatives	1997–98: Anticorruption Commission	The Commission became operational in 1998 but had little effectiveness because it lacked government cooperation.
Federation government	September 1999: Commission of International Legal Experts	The Commission's mandate was to examine the nature and causes of corruption in the Federation and recommend measures to improve the Federation's anticorruption efforts. The Commission produced the final report in February 2000 and disbanded.

Implementor	Date established/activity	Comments
Bosnian government—agreed by Prime Ministers Bicakcic and Dodik	November 1999: Joint-entity Anticorruption Coordination Group	As of May 2000 the group had not been established.
Federation government—House of Representatives	December 1999: Anticorruption strategy	Working groups are developing an anticorruption strategy and implementation plan for the Federation's House of Representatives. As of March 2000, the Federation government had completed the strategy for fighting corruption and was preparing to send it for parliamentary approval. According to the Deputy Minister of Justice, this document is the first comprehensive strategy document created by Bosnians.
International efforts		
European Commission	1996: Customs and Fiscal Assistance Office	Office was established to help Bosnia form a coherent customs system at the national and entity levels. The office has assisted in passing needed customs legislation and identified incidents of corruption and illegal activities resulting in the loss of customs duties and tax revenues. As recommended by the Peace Implementation Council in December 1997, the office expanded to include assistance in the taxation field.
Office of the High Representative	April 1998: Anti-Fraud Unit	Unit was created at the request of the December 1997 Peace Implementation Council in Bonn, Germany, to combat corruption and organized crime. The unit works with local authorities to investigate and prosecute significant fraud and corruption cases.
Office of the High Representative	February 1999: Anticorruption strategy	Strategy addresses systemic and case-level corruption. The systemic approach is based on four strategic "pillars": (1) eliminating opportunities, (2) transparency and reporting, (3) control and penalties, and (4) education and public awareness. Reform is underway or planned in four major sectors: (1) public revenue, (2) the rule of law, (3) institutions, and (4) public awareness.
Office of the High Representative	July 1999: Judicial reform strategy	Strategy called for by the 1998 Madrid Peace Implementation Council. The strategy focuses on all aspects of the criminal justice system, including police investigations, prosecutions, and trials.
Office of the High Representative	September 1999: Anticorruption and Transparency Group	Group established to reinvigorate international anticorruption initiatives. Meets monthly.
Office of the High Representative	Judicial Reform Coordinating Group	Group established to develop a coordination structure for the international community's efforts in the judicial reform area. The group meets every 4 to 6 weeks to discuss progress and problems and recommend changes in the judicial reform strategy.
Office of the High Representative	On-going: Imposed laws	Examples include three laws imposed in July 1999–the amendments to the law on the Supreme Court of the Federation, the amendments to the law on the Federal Prosecutor's Office, and the law on special witness identity protection proceedings.

Implementor	Date established/activity	Comments
Office of the High Representative	On-going: Remove officials for anti-Dayton Agreement activities	Example: In November 1999, 22 officials were dismissed. Among the 22, 9 were mayors, 2 were cantonal ministers, and 1 was a cantonal governor.
Organization for Security and Cooperation in Europe	1999: Municipal infrastructure finance and implementation training	Direct assistance is provided to local governments to improve transparency and accountability and to increase citizens' participation in policy-making at the local level.
Organization for Security and Cooperation in Europe	1999-2000: Prosecutor training	Prosecutors are trained with the goal of strengthening their role in the Bosnian legal system.
Stabilization Force	December 1998: Entity armed forces Inspector Generals Office	Office established to professionalize the entities' armed forces. The focus of investigations is professional military ethics and leadership. To date, several noncompliant officers have been removed, reassigned, or suspended as a result of the investigations of the office.
Stabilization Force	On-going: Intelligence gathering, raids	SFOR's intelligence gathering led to the October 1999 raid on Bosnian Croat facilities in west Mostar, Operation WESTAR. During the operation, SFOR seized large quantities of weapons, pirated software, counterfeiting equipment, and intelligence information.
Swedish International Development Agency/Swedish National Audit Office	June 2000: Audit institution development	Long-term institutional support for the development of supreme audit institutions. As of June 2000, auditors general and deputies had been selected for Bosnia at the state level. Efforts were underway to select an auditor general for each entity.
Transparency International	Ongoing: Establishment of local chapter	Transparency International officials visited Bosnia three times between December 1999 and March 2000 to identify Bosnians interested in establishing a local chapter.
United Nations	December 1995: International Police Task Force	Annex 11 of Dayton Agreement established the international police assistance program to, among other things, monitor, observe, and advise on law enforcement matters.
United Nations	1998: Judicial System Assessment Program	Program monitors and assesses the court system in Bosnia in three main areas: technical, political, and institutional. Achievements include the creation of a database on all courts and prosecutors within Bosnia.
World Bank	1998: Public finance structural adjustment credit	Provides policy advice and assistance in public finance reforms. Examples are the development of a budgetary strategy aimed at improving fiscal efficiency and control and the establishment of a public audit system to promote transparency and accountability in the government.
World Bank	May 2000: Corruption study implemented	The Bank extended an invitation to the Bosnian government to conduct a study of the root causes of corruption in Bosnia. The international community will be asked to finance this study, and all three ethnic groups will be asked to sign on to the study. Study was implemented in May 2000.

Implementor	Date established/activity	Comments
U.S. Efforts		
Justice Department	1996: International Criminal Investigation Training Assistance Program	Program provides training and equipment to develop the police forces in both entities. The program includes institutional development, police academy development, criminal investigations, forensic capacity, and specialized training. Internal affairs units have been established with this assistance.
Justice Department	1998: Overseas Prosecutorial Development, Assistance, and Training with the American Bar Association's Central and East European Law Initiative	Purpose is to train judges, prosecutors, and police in reformed criminal laws adopted by the Federation in 1998. Training given in fighting organized crime and investigating and prosecuting public corruption. Works on programs to strengthen the independence and efficiency of the judiciary.
Justice Department	2000: Federal Bureau of Investigations	FBI agents are examining public sector corruption in Bosnia. They will also investigate other high-profile cases and prepare the cases for trial.
U.S. Agency for International Development (USAID)	March 1998: Anticorruption study/strategy	USAID believes it is still relevant and thus has not updated it.
U.S. Agency for International Development	On-going: Payments bureaus reform	USAID chairs the multi-donor advisory group that assists in payments bureau reform. Program goals include the development and implementation of standards to permit banks to provide payment services; the abolition of overnight ceilings on cash holdings and the requirement that businesses deposit cash with the payments bureaus; the transfer of tax collection and Treasury functions to the Ministries of Finance; and the transfer of statistical functions to other institutions.
U.S. Agency for International Development	On-going: Privatization effort	USAID played a key role in drafting and facilitating the passage of privatization laws and the establishment of key privatization institutions. Conducted training for government officials, enterprise managers, and the media on the privatization process in both the Federation and the Republika Srpska. Also conducting a privatization education program countrywide to increase public awareness of and confidence in the process.
State Department	Ongoing: Training courses through the Bureau of International Narcotics and Law Enforcement Affairs	State provides specialized training courses for law enforcement personnel. For example, the U.S. Customs Service is providing a course in money-laundering control.
State Department	September 1999: U.S. interagency, Anticorruption task force	Task force focuses on strengthening the existing anticorruption mechanisms in Bosnia, such as the Office of the High Representatives Anti-Fraud Unit.
Treasury Department	On-going	Treasury assistance in budget and taxation reform, banking privatization, and payments bureaus reform. Has also developed a program to establish the efficient management of public funding through transparent budgets and accountability.

Comments From the Department of State

Note: GAO comments supplementing those in the report text appear at the end of this appendix.

United States Department of State

Chief Financial Officer

Washington, D.C. 20520-7427

June 2, 2000

Dear Mr. Hinton:

We appreciate the opportunity to review your draft report "BOSNIA PEACE OPERATION: Crime and Corruption Impedes the Success of the Dayton Peace Agreement," GAO/NSIAD-00-156, GAO Job Code 711473.

The Department of State comments are enclosed for incorporation as an appendix to the final report. Technical changes were provided to your staff for incorporation as appropriate.

If you have any questions concerning this response, please contact Mr. Michael Dovilla, Office of Bosnia Implementation, Bureau of European Affairs, at (202) 647-4642.

Sincerely,

Bert T. Edwards

Enclosure:

As stated.

cc:
GAO/NSIAD – Mr. Bruno
State/EUR/BI – Mr. Dovilla

Mr. Henry L. Hinton, Jr.,
Assistant Comptroller General,
National Security and International Affairs,
U.S. General Accounting Office.

Department of State Comments on the GAO Draft Report
"BOSNIA PEACE OPERATION: Crime and Corruption Impedes the Success of the Dayton Peace Agreement," GAO/NSIAD-00-156,
GAO Job Code 711473

See comment 1.

While we welcome the report's conclusion that the U.S. has established effective safeguards on its assistance to Bosnia and Herzegovina (BiH), we disagree with the report's implication that the existence of corruption in BiH suggests that assistance over the past four and a half years has been wasted and that a reassessment of the U.S. approach to assisting BiH is needed.

See comment 2.

Along with other donors, the U.S. initially focused on the urgent priority of rebuilding a devastated country. Reconstruction was the area to which the bulk of resources initially went. By 1998, a sufficient amount of reconstruction had occurred to enable a shift in priorities toward reforms in the economy, judicial system and central state institutions. As a result, the U.S. government reassessed its assistance and redirected its efforts to economic, political and judicial reform. Our current assistance strategy reflects the U.S. government's continual reassessment of priorities. There is no need for a comprehensive reassessment.

See pp. 26-32.

In fact the U.S. Government has now made tackling corruption and fraud one of its main priorities, as reflected in the appointment of an interagency Anti-Corruption Task Force for BiH in September 1999 headed by the U.S. Department of State. The task force's goals include both structural reforms in BiH and criminal prosecution. U.S. programs established to tackle corruption include an array of economic reform programs coupled with assistance to public prosecutors, assistance in criminal law reform as well as FBI agents sent to help with criminal investigations. This U.S. effort complements strong international initiatives, including stepped up efforts by the Office of the High Representative in BiH which coordinates anti-corruption activities in BiH. Most recently, the Peace Implementation Council in May highlighted the imperative for institutional reforms to end corruption. Bosnian authorities are brought into all these fora and pressed to take further initiatives on their own.

See comment 3.

We disagree with the report's assertion that Bosnians have categorically and systematically refused to cooperate in fighting corruption. While certain government officials oppose reform, some more moderate officials have cooperated with the

- 2 -

international community and others have been pressured into cooperation. For example, criminal code reforms were adopted in the Federation and significant judicial reform legislation was passed in the RS.

See comment 1.

Reassessment: By 1998, the U.S. government undertook a broad reassessment of its assistance, resulting in the following:

- Overall SEED assistance levels dropped from $258 million in FY 1998 to $180 million in FY 1999, and $100 million in FY 2000. The FY 2000 level represents a 61 percent drop in two years, and is $30 million below the ceiling set by Congress.
- Reconstruction assistance dropped in the same period from $61 million to $50 million to zero.
- Funding for business lending dropped from $110 million to $50 million to zero. We are developing proposals to use undisbursed funds and reflows from this program.
- Budget support constituted under 2 percent of assistance during 1996-2000, and was terminated after a $17 million appropriation of FY 1999 ESF.
- While assistance levels dropped drastically, we have maintained funding for economic reform at around $24 million annually. This funds programs such as improving budget transparency, closing out party-controlled payments bureaus, and preparing enterprises for privatization.
- Our funding for judicial reform has increased drastically in percentage and dollar terms, from $780,000 in FY 1998 to $5 million in FY 2000. This includes support for building up vetted strike forces, strengthening public prosecutors, and establishing an anti-fraud unit at the Office of the High Representative.

See comment 4.

Our heightened emphasis on economic and judicial reform supports U.S. advisors in the field to revise laws, reform economic and judicial institutions and re-train officials. Although the outputs of such technical assistance may be less tangible than reconstruction efforts, we believe that they will achieve measurable reforms over time. At least as important as dollar levels is the political commitment to reform. As a result of U.S. leadership, the international community has taken a much more aggressive stance with Bosnian authorities in exacting reform commitments.

See comment 5.

Conditionality: We agree with conditionality in principle and have been encouraging other donors and international

- 3 -

financial institutions to apply conditionality. However, with the phase-out of U.S. reconstruction assistance, we now put most of our money in programs (minority returns, rule of law, media, economic reforms) unwelcome to the nationalist establishments. The threat to withdraw such aid may not be an effective tool as its would be welcome by, and reward, hard-line forces that oppose reforms. However, we will continue to use our influence with other donors and international financial institutions to apply conditionality where appropriate.

See pp. 40-41.

Budget Support: We agree that direct budget support should be carefully evaluated because of the difficulty in establishing firm controls over its use. The U.S. is no longer providing fresh budget support, but the modest amounts it did give were targeted at specific goals. Budget support during 1998-99 for the RS bolstered a moderate government and helped prevent Belgrade-supported parties from deterring Dayton implementation. Maintaining a moderate RS government has helped remove media from the control of Serb nationalist parties, begin large-scale returns of Bosniaks and Croats to the worst areas of ethnic cleansing in the war and promote strengthened RS-Federation cooperation on a broad range of issues.

We look forward to working closely with your staff in the future as we continue to reassess the effectiveness of the programs and the appropriateness of overall funding levels in light of the evolving situation in Bosnia.

The following are GAO's comments on the Department of State's letter dated June 2, 2000.

GAO Comments

1. We do not believe our report implies that because of corruption in Bosnia assistance over the past 4-1/2 years has been wasted. It points out that the United States and the international community focused a large part of their aid on physical reconstruction. We did not evaluate the large expenditure of funds to rebuild Bosnia's physical infrastructure but acknowledge that this phase of the assistance program has largely been completed. This progress necessitates an assessment of the direction of future aid. We agree that State completed an assessment and made decisions on future funding directions by 1998. Our report, however, focuses on U.S. and international efforts over the past 4-1/2 years to address crime and corruption and to develop a functioning judiciary in Bosnia.

2. We modified our recommendation to make clear that we believe that the strategy for providing assistance should be reevaluated.

3. Our report states that crime and corruption pervade Bosnian political, judicial, and economic systems and that Bosnian leaders have not demonstrated a desire to eliminate corruption and develop a society based on the rule of law, despite 4-1/2 years of international and U.S. efforts to redress these problems, including more emphasis in the past 2 years. State said that while certain government officials oppose reform, some more moderate officials have cooperated with the international community and others have been pressured into cooperating. We modified our report to add this perspective; however, this does not alter our basic assessment that crime and corruption pervade Bosnian political, judicial and economic systems.

4. We agree with State on its point that as a result of U.S. leadership, the international community has taken a much more aggressive stance with the Bosnian authorities in exacting reform commitments. However, there is no evidence that these efforts have resulted in a change in Bosnian desire to eliminate corruption.

5. We recognize the risk of withdrawing U.S. aid, but have suggested that State reevaluate its strategy for addressing this problem so that there will be a better likelihood that the broader goals of the Dayton Agreement will be met. We note that the U.S. Ambassador to Bosnia is

successfully conditioning U.S. aid to elicit better cooperation in economic reform efforts. This success indicates that more extensive use of conditionally is justified.

Comments From the U.S. Agency for International Development

Note: A GAO comment appears at the end of this appendix.

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

June 9, 2000

Mr. Henry L. Hinton, Jr.
Assistant Comptroller General
National Security and International Affairs Division
U.S. General Accounting Office
441 G Street, N.W. - Room 4039
Washington, D.C. 20548

Dear Mr. Hinton:

I am pleased to provide the U.S. Agency for International Development's (USAID's) formal response on the draft GAO report entitled, "Bosnia Peace Operations: Crime and Corruption Impedes the Success of the Dayton Peace Agreement (May 2000)."

The GAO report finds that there is "no evidence that assistance is being lost to large-scale fraud or corruption in Bosnia" and that USAID's method of tracking and auditing of the $22 million in budget support provided to the entity government of the Republic of Srpska is "rigorous." We feel that the U.S. taxpayers' dollars, safeguarded by USAID's strenuous monitoring systems, have been the base from which the Bosnians have begun to build a new nation based on democratic principles and a market economy (and we are pleased that it was so noted).

Addressing the issue of corruption has been a critical component of USAID's Bosnia and Herzegovina project portfolio over the past four and half years. Taking advantage of the linkages between its economic reform and democracy building portfolios, USAID has focused on an institutional approach to fighting corruption, re-structuring and reforming the economic sector and developing, strengthening and sustaining civil society. Strengthening the judicial institutions and insulating judges and prosecutors from undue influence will bring credibility to the system and is a principal focus of the USG's efforts. Likewise, training journalists in the art of aggressive and fact-based research will hone their skills in uncovering and reporting on corruption.

The report suggests that the "elimination of corruption in Bosnia" is a goal of international assistance; we believe that is an unrealistic expectation. Rather, our goal is to develop a regulatory and legal framework and strengthen its enforcement through the development of sustainable regulatory agencies, an independent judiciary, and a free media to encourage political will to battle crime and corruption. Our real long term goal in Bosnia, from this stand point, is to build the political will to

1300 PENNSYLVANIA AVENUE, N.W.
WASHINGTON, D.C. 20523

no longer accept and condone the presence of corruption. Please find attached a paper describing in detail USAID's efforts in anti-corruption through its various programs. I would like to just highlight a few issues here, however.

USAID/Bosnia is presently re-assessing its country strategy and will present it to AID/Washington for approval in December 2000. The information contained in the GAO report will be taken into consideration in the development of the country strategy. However, I would caution invoking broad-based conditions on USG assistance to Bosnia. Broad conditions would be detrimental to USAID's technical assistance. Specifically, USAID's engagement in dismantling the powerful and corrupt payments bureaus, establishing bank regulatory agencies and guiding and overseeing privatization must not be held hostage to the behavior and actions of the government. To do so would only play into the hands of the entrenched political and economic interests who view USAID's assistance as threatening their political control.

I would like to bring three Bosnian institutions or groups of dedicated individuals to your attention which are functioning particularly well within their important realm of responsibility and implementing the regulations and laws to root out corruption: the employees and directors of the Federation and Republic Srpska Banking Agencies and the Tuzla Financial Police. In a country fraught with crime, these individuals have acted against political and economic vested interests at the highest levels of government at risk to their own personal safety and that of their families. It is their aggressive action and fact-based investigations that have given these three organizations credibility in the eyes of the public--now it is up to the government and courts to act.

Thank you for the opportunity to respond to the GAO draft report and for the courtesies extended by your staff in the conduct of this review.

Sincerely,

Richard C. Nygard
Acting Assistant Administrator
Bureau for Management

Attachment:
USAID Cross-cutting Corruption Program

The following is GAO's comment on the U.S. Agency for International Development's letter dated June 9, 2000.

GAO Comment

We agree that the "elimination of corruption in Bosnia" is an unrealistic goal and have changed our report to indicate a need to address corruption.

Comments From the Department of Defense

THE UNDER SECRETARY OF DEFENSE
2000 DEFENSE PENTAGON
WASHINGTON, DC 20301-2000

POLICY

MAY 30 2000

Mr. Benjamin F. Nelson
Director, International Relations and Trade Issues
National Security and International Affairs Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Nelson:

This is the Department of Defense (DoD) response to the GAO draft report, "BOSNIA PEACE OPERATION: Crime and Corruption Impedes the Success of the Dayton Peace Agreement," dated May 15, 2000 (GAO Code 711473/OSD Case 2004).

The Department of Defense has reviewed the draft report and generally concurs with your findings. We agree with your overall assessment that crime and corruption is endemic in Bosnia and impeding the economic, political, and judicial reform aspects of the Dayton Peace Agreement. However, we should not overlook the accomplishment of other benchmarks, including military stability.

Additionally, we request that you stress in your recommendations the importance of establishing rule of law and the need for further judicial reform as key to enforcing the reduction of crime and corruption. As your report states (p. 17), "An inadequate judicial system precludes successful prosecution of government fraud, corruption and complex white-collar crime." Therefore, any efforts made to thwart corruption must include more stringent judicial enforcement efforts.

Further suggested substantive comments, technical corrections and other comments for accuracy were provided separately to GAO staff. The Department appreciates the opportunity to comment on the draft report.

Sincerely yours,

Walter B. Slocombe

Objectives, Scope, and Methodology

At the request of the Chairman, the Ranking Minority Member, and a Member of the House International Relations Committee, we examined (1) how organized crime and public sector corruption affect the successful implementation of the Dayton Agreement in Bosnia, (2) whether the international community's anticorruption and judicial reform efforts have improved Bosnia's law enforcement and judicial systems, and (3) whether international assistance is being safeguarded and is being used by Bosnia in place of domestic revenues lost due to crime and corruption.

To address these objectives, we conducted comprehensive interviews with and collected and analyzed documentation from key U.S. government officials engaged in the reconstruction of Bosnia, including officials at the Departments of State, Defense, Justice, and Treasury; USAID; and the American Bar Association's Central and East European law initiative in Washington, D.C. Additionally, we reviewed reports prepared by the International Management Group (an intergovernmental organization dedicated to the rehabilitation/reconstruction of the infrastructure of Bosnia), Transparency International, and the Commission of International Legal Experts on corruption and anticorruption efforts in Bosnia-Herzegovina.

We also conducted 2 weeks of fieldwork in Bosnia-Herzegovina, where we interviewed over 40 members of the international community and Bosnian government officials, such as the Federation's Prime Minister and Finance Minister. Additionally, we interviewed officials from the Federation Banking Agency and the Republika Srpska's Ministries of Finance, Interior, and Customs Administration. We collected and analyzed documents such as anticorruption and judicial reform strategies provided to us by the Department of Justice; USAID; the U.S. Embassy in Sarajevo, Mostar, and Banja Luka; the Organization for Security and Cooperation in Europe; NATO's Stabilization Force; the European Commission Customs and Fiscal Assistance Office; the International Monetary Fund; the World Bank; the U.N. Mission in Bosnia; the Office of the High Representative; the European Bank for Reconstruction and Development; the European Commission Monitoring Mission; and the International Crisis Group.

We conducted our review from December 1999 through May 2000 in accordance with generally accepted government auditing standards.

GAO Contact and Staff Acknowledgments

GAO Contact

F. James Shafer, (202) 512-6002

Acknowledgments

In addition, David M. Bruno, E. Jeanette Espinola, and Hynek P. Kalkus made key contributions to this report.

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