

**Latvia's Contribution
to the Regular Report from the Commission
on Latvia's Progress Towards Accession
(National Progress Report)**

Riga 1999

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A. INTRODUCTION

a) Preface

The context of the Progress Report

The European Commission's Progress Report in November 1998 highlighted Latvia's achievements in implementing the EU Copenhagen criteria. These results have been achieved through a pragmatic and consistent approach. Since the restoration of independence, Latvia has pursued a determined policy of integration into the European Union. This policy is a catalyst for the reform process in Latvia.

The political maturity of Latvia's electorate was confirmed during the elections on 3 October 1998. Only six parties from 21 lists were elected in the Parliament (*Saeima*). All of them fully support Latvia's integration into the European Union. The Government, approved on 3 December 1998, provides continuity of EU integration policy. The election of the next State President, Mrs Vaira Vike-Freiberga, on 17 June 1999, confirms sustainability of democratic values in Latvia.

One of the main policy aims of the Government is to create a unified and integrated society in Latvia. After adoption of the Framework document of the Integration Programme, in 1999 a broad public debate was organised. More than 25.000 persons took part in different events of the debate.

The rate of naturalisation has accelerated considerably after the entry into force of the amendments to the law "*On Citizenship*" in November 1998. Amendments supported by the 3 October 1998 referendum give practically all non-citizens of Latvia the opportunity to apply for naturalisation. 8308 persons requested citizenship between November 1998 and May 1999, in comparison to 2094 applications received in the first six months of 1998. This upward trend continues. In April and May 1999 the Government allocated additional funding (37.000 Lats) to the Naturalisation Board to increase operational capacities. The Government continues to implement the 'National Programme for Latvian Language Training' with the assistance of EU PHARE funding. In December 1998, the second 2-year phase of the Programme was started. Already in the first half of 1999 alone more than 8.500 persons attended Latvian language courses.

The macroeconomic situation remains stable. Economic growth continued in 1998 despite economic pressure on Latvia caused by a full-scale economic crisis in most of the CIS. The Government remains committed towards implementation of prudent stabilisation policies in compliance with the Joint Assessment on Economic Policy Priorities.

GDP growth in 1998 was 3.6%. The increase in GDP was primarily driven by investment, which grew at a steady rate of 12%. Inflation has continued to fall, in average reaching just 4.7% in 1998. While exports to the CIS declined by 29.4%, exports to the European Union increased by 27.3%, encouraging further trade diversification.

Both service and industrial sectors showed positive growth in 1998. The service sector continued booming in the beginning of 1999, accompanied by strong growth in construction. The production output of clothes, ships, wood products and other goods with basic sales markets in the west continues growing.

The continued inflow of investment has been facilitated by improved structural conditions for domestic lending and an improved legal and regulatory environment of business activities. The

overall level of credits to enterprises and households grew by 77.4% in 1997, and a further 49.6% in 1998. The fall in capital base after the Russian financial crisis has ceased.

In 1998 the trade and current account deficits for Latvia amounted to 17,6% and 11% of GDP. The ongoing restructuring of enterprises as well as economic reorientation will help to cope with the problem of current account deficit in the medium term.

The privatisation process is almost complete. 97% of the former state-owned enterprises are now in private hands. The purchase agreements stipulated retention of 7704 jobs.

Foreign direct investment continued to grow, accelerating the restructuring process. The transport and communications sector has accumulated 31% of the FDI; manufacturing and financial sectors received 20% and 23% of the total FDI. In manufacturing, the processing and chemical sub-sectors attracted the most foreign direct investment.

Standard & Poor's "BBB" rating for long-term foreign currency debt assigned in June 1999 is an expression supporting international investor confidence.

The Government continues to increase the institutional and administrative capacity of its central and local administration. Public administration reform takes fully into account the need for applying and enforcing the *acquis* effectively. An institution building plan now is part of the National Programme for the Integration into the European Union. Structural reforms of public administration are being implemented in compliance with public administration medium-term strategy. An important development is the creation of an internal audit system for the whole central administration. Latvia continues to strengthen its institutions responsible for regional policy and cohesion.

To enhance the political responsibility for the integration process as a whole, a special political post, Deputy Prime Minister for EU Integration, has been created. The Deputy Prime Minister is the Head of the European Integration Council. The horizontal structure for co-ordination of EU integration is stable and well developed. Effective management is ensured by the European Integration Council, the Council of Senior Officials, European Integration Bureau and the Ministry of Foreign Affairs. Structures responsible for EU policy implementation and co-ordination operate in each line ministry.

b) Relations between the European Union and Latvia

The Enhanced Pre-Accession Strategy

The Association Council noted that major progress has been made in dealing with implementation of the Accession Partnership priorities. Latvia has prepared the enhanced Third National Programme for European Integration (Adoption of the *Acquis*). The Programme assesses the status of Latvia's preparation for membership in each sector. The Programme includes budget estimates so that EU assistance may be targeted in a manner which will complement national budget allocations.

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

Recent Developments in Bilateral Relations

The framework of the Europe Agreement represents an effective means for Latvia to prepare for EU membership.

The Association Council has proven itself to be an effective instrument for driving preparation work forward. The Council held its second meeting in February 1999. The EU side noted that the Association mechanisms have reached their cruising speed and allow for fruitful co-operation. The Council welcomed the favourable developments in Latvia, in particular in the macroeconomic field, in foreign direct investments, in privatisation, and underlined important steps towards strengthening the public administration.

During its third meeting in January 1999, the EU-Latvia Joint Parliamentary Committee welcomed the Commission's Regular Report, which clearly indicated that Latvia had made substantial progress in its preparations for EU membership.

Subcommittees established under the Europe Agreement allow for proper evaluation of Latvia's success in realising alignment with EU legislation and commitment to EU principles and values. As a result of successful monitoring and implementation of Europe Agreement obligations, Latvia has made good progress in harmonising its legislation and in establishing implementation structures, particularly in the area of competition, standards and certification.

The free trade regime with the EU under the Europe Agreement has enhanced Latvia's economic capacity to cope with competitive pressures within the EU. The EU is the main trading partner for Latvia, and bilateral EU-Latvia trade has been constantly growing. Compared to 1997, when Latvia's exports to the EU were 48.9% of the total and imports 53.2%, 1998 saw a significant increase in the EU share. At present 56.6% of Latvia's exports are heading for the EU, and Latvia takes in 55.3% of her imports from EU member states. These statistics suggest that Latvia has already achieved a high degree of trade integration with the EU.

Only four candidate countries have entered into negotiations on the Protocol on European Conformity Assessment. In October last year, Latvia was invited to start these negotiations due to the substantial progress in harmonisation of Latvia's internal market legislation with the *acquis*. The relevant Latvian legislation will be harmonised with EU norms.

The participation in Community programmes gives Latvia the possibility to acquire an experience of co-operation of EU countries. Latvia is a full member of the *Socrates*, *Leonardo da Vinci* and *Youth for Europe* programmes and in the cultural programme, *Raphael*. Participation in the "5th Framework Programme in Research and Development" is a major challenge for the nearest future.

Since the beginning of the bilateral screening process in March 1999, Latvian legislation has been screened in significant sectors such as Free Movement of Capital, Free Movement of Goods, Fisheries, Industrial Policy and others. During the meetings, in most cases the EU side has expressed satisfaction with the quality of newly adopted legislation and the timetable for future legislation in Latvia. Much has yet to be done in approximation of legislation. Nevertheless, no major problems in the adoption of the *acquis* are expected.

B. CRITERIA FOR MEMBERSHIP

1. Political criteria

Introduction

The Saeima elected the President on 17 June 1999. The new Latvian President is the first woman elected in this post in the Central and Eastern Europe. Since the amendments to the “*Citizenship Law*” entered into force on 10th of November 1998, the number of applications for naturalisation has increased significantly. The naturalisation procedure has been simplified and improved, and the Naturalisation Board has received additional state funding for the accomplishment of its tasks. The “*National Programme for Language Training*” is implemented effectively. A Society Integration Programme is under preparation. A consistent progress has been made in the implementation of the public administration reform and strengthening of the judiciary.

1.1 Democracy and the Rule of Law

Parliament

All six parties elected in the Latvian Parliament (*Saeima*) in October 1998 have announced their full support for Latvia’s integration to the European Union. The powers of the Parliament are respected accordingly. The opposition plays a full and active role in its activities.

The Saeima elected the President on 17 June 1999. The new Latvian President is the first woman elected in this post in the Central and Eastern Europe.

The European Affairs Committee of the Saeima continues to play the leading role in the adoption of significant EU - compatible legislation in priority areas.

The Executive

The Government and other institutions of public administration continue to operate in a steadily improved way.

The Saeima approved the Government on 3 December 1998. Three centre-right political parties form the governing coalition, and a separate agreement was concluded with the Social Democrats.

Public administration reform is being further implemented. Functional reorganisation of the public administration institutions is based on a methodology tested by the World Bank in the countries of Central and Eastern Europe. Internal audit units have been established within the Ministry of Finance, the Treasury and the State Revenue Service. Similar units will be established in all ministries.

The post of a Minister Responsible for the Public Administration Reform was established in June 1999. The Public Administration Reform Bureau is now subordinated to the new Minister.

The judicial system

Reform of the judicial system continues to strengthen the independence of the judiciary, to improve efficiency and impartiality of the administration of justice and to prepare the judiciary for EU membership.

In November 1998, important amendments to the basic laws of the judicial system - the law "*On Judicial Power*" and the law "*On the Disciplinary Liability of Judges*" - came into force. An increase in the basic salary for judges was approved and implemented by this law. Now judges receive wages at a level equivalent to that of senior civil servants. Impartiality in the evaluation of judges' work has been ensured. The amendments also ensure higher standards for qualifications of judges, provide more flexibility in the organisational administration of the system of courts and increase the role and powers of self-governing institutions of the judiciary - the Disciplinary Board of Judges and the Judicial Qualification Board. The new system ensures a more objective system of evaluation and granting of judicial qualification degrees. Thus the judges have been given further stimulus to promote their professional skills and qualifications, *inter alia* by participating in the programmes prepared by the Judicial Training Centre in co-operation with the Ministry of Justice. Within the framework of the PHARE Programme on Judicial reform, training for almost all Latvian judges in basic European law is being planned in co-operation with the European Law Academy in Trier. A separate supervisory body, the Judicial Training Council, is at the stage of creation.

In addition, a new law on the judicial power and courts' organisation is being drafted.

A new "*Law on Civil Procedure*", adopted in 1998, is in force since 1 March 1999. The law ensures speediness of the court proceedings and reduces delays by providing stricter conditions on i.a. non-appearance in court hearings and by regulating conditions for lawsuits in absentia. Court statistics now show that procedural delays have considerably decreased after these reforms. The new Code of Civil Procedure has abolished the time limit for judges; therefore the apparent inconsistency will no longer exist.

In the framework of the PHARE project "Court System Reform", another programme provides for creation of a court information system, the prototype of which will be submitted for approval in September 1999. The creation of a countrywide court computer network has started. Several regional courts are currently equipped with computers connected by local area networks; appropriate software is being elaborated.

Enforcement of judgements in civil matters is improving. Following the experience of France and Belgium, Latvia is reforming the court bailiff system with the aim of achieving a status of a liberal legal profession similar to notaries. A draft law "On Sworn Court Bailiffs" is being prepared. A programme for training of court bailiffs is underway.

The death penalty issue in Latvia has been successfully solved. The Saeima the 6th Additional Protocol to the European Convention on Human Rights, which came into force on 1 June 1999, thus completely abolishing the death penalty and substituting it by life imprisonment.

For the sake of ensuring the human rights of prisoners, reform of the prison system is a government priority. In October 1998, the "*Penitentiary Code*" was amended in order to improve the mechanisms for carrying out sentences, for the establishment of the Probation Service and for application of alternative non-confinement punishments. The Saeima in the first reading in November 1998 already approved the new Penitentiary Law, after an examination by experts of the Council of Europe. The Ministry of Interior is now performing supervision of prisons and, by the end of 1999 will transfer supervisory authority to the Latvian Ministry of Justice.

Anti-corruption measures

The prevention of corruption is among the priorities of the Government. A Corruption Prevention Programme is being implemented. Under the leadership of the Minister of Justice the Corruption Prevention Council shapes and implements national policy in the sphere of prevention of corruption. Active involvement by civil society plays an important role in corruption prevention. Two major conferences run jointly by the Corruption Prevention Council and the World Bank were held in Latvia in June 1998 and in February 1999. In January 1999, Latvia signed the “*European Criminal Law Convention on Corruption*”.

A new “*Criminal Law*” is in force since 1 April 1999. The law envisages the introduction of the notion of a “criminal misdemeanour” alongside with the notion of a “crime”. A uniform age limit at which criminal liability sets is being established, norms on kinds and types of complicity have been improved, and important changes are being introduced in the system of criminal penalties. The new Criminal Law contains improvements not only from the point of view of modern criminal law, but also regarding the *acquis*. A number of actions have been criminalised, e.g. corruption in the private sector, such as criminal liability for the abuse of power, as well as commercial bribery, committed by a representative or an authorised person of a non-governmental company or organisation.

The “*Corruption Prevention Law*” contains the main legislation applying to this subject. In 1998, this law was amended to further restrict corrupt activities and the “*Code of Administrative Misdemeanours*” was strengthened.

The structure of the Corruption Prevention Division of the State Revenue Service (SRS) has been expanded and the qualifications of its employees have been raised through special training programmes. The SRS and the State Police are co-ordinating co-operation in the combat of organised crime. A Department of Financial Analysis, Auditing and Control has been established within the State Police in order to uncover corruption.

In June 1998, the law “*On Prevention of Legalisation of Proceeds from Crime*” entered into force. To implement the law, a Control Office working under the supervision of the Prosecutor’s Office was established. In July 1998, the Government adopted the regulation “*On Features of Unusual Financial Transactions*”. In October 1998, Latvia ratified the “*European Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime*”.

1.2 Human Rights and the Protection of Minorities

In October 1998 the Saeima adopted a new Chapter of the Constitution (Satversme): “*Fundamental Human Rights*”. Thus the protection of human rights and fundamental freedoms has been elevated to a constitutional level.

In April 1999 the Saeima ratified the 6th Protocol of the European Convention for the Protection of Human Rights and Fundamental Freedoms, thus abolishing the death penalty in Latvia.

Civil and Political Rights

In February 1999 the law “*On the Status of Stateless Persons*” was adopted by the Saeima.

In July 1998 the law “*On the Protection of the Rights of the Child*” came into force. The system of protection of the rights of children is re-organised and developed in the process of implementation of the Law.

The Government approved Latvia's accession to the Convention relating to the Status of Stateless persons in April 1999.

In October 1998 the law "*On Access to Information*" was adopted. The Law provides the public with guaranteed access to information at the disposal of state administrative and municipal authorities.

In October 1998, the "*Penitentiary Code*" was amended in order to improve the mechanisms for carrying out sentences and for the establishment of the Probation Service and for application of alternative non-confinement punishments. The new "*Penitentiary Law*", after an examination by experts of the Council of Europe, has been already approved by the Saeima in the first reading in November 1998.

In 1998 Latvia continued to implement a far-reaching prison reform, including reconstruction of the Central Prison and training of professional guards for *Grīva* prison. The prison administration continued to strengthen co-operation with NGO's, which organise education programmes, radio broadcasts and publish a prison newspaper.

In June 1998, the European Convention for the Prevention of Torture and Inhuman or Degrading Treatment or Punishment entered into force in Latvia. Representatives of the Committee on the Prevention of Torture visited Latvia in January - February 1999 to study the situation in closed institutions, such as army bases, psychiatric hospitals, police stations and an asylum seeker detention centre.

In January 1998, the Government set up the Government Agent's office. The main tasks of the Government Agent will be representation of Latvia to the European Human Rights Court and preparation and submission of National Reports to the International Human Rights Institutions. In March 1998 the Government adopted the regulations "*On the representation of the Government to the International Human Rights Institutions*".

Latvia is an elected member of the United Nations Human Rights Commission for the period 1999 - 2001.

Economic, Social and Cultural Rights

The results of the elections in October 1998 led to an increase in the number of women parliamentarians from 8 to 17 and an increase in women ministers from 2 to 5 (Justice, Economy, State Revenue, Culture, State Minister for Environment). The newly elected State President is a woman.

In December 1998, the Government decided to designate a unit within the Ministry of Welfare responsible for gender equality issues. This unit has been operating since March 1999. Thus a key recommendation of the Beijing Platform for Action has been implemented.

Minority Rights and the Protection of Minorities

State-financed education is available in eight minority languages - Russian, Polish, Jewish, Ukrainian, Estonian, Lithuanian, Roma (Gypsy) and Belorussian. State-financed tertiary education is provided in Latvian. A number of private educational institutions with languages of instruction other than Latvian exist, and they may receive financial assistance from the State.

A major development in the area of education was the adoption of a "*Education Law*" in October 1998. In accordance with the Law, schools with language of instruction other than Latvian will choose either to gradually switch over to Latvian as the language of instruction or to start

implementing minority education programmes. These programmes will be developed by the educational establishments themselves using as the basis the model general education programmes prepared by the Ministry of Education and Science. There are four models which differ with regard to the proportion of classes to be held in Latvian and minority languages respectively. The schools themselves will choose the model which suits best the interests and language skills of their students. In compliance with the “*Education Law*”, the status of educational programmes for minorities has been established and funding of these programmes from the state and municipal budget is guaranteed in general education.

The “*Education Law*” fully corresponds to international human rights standards. Mr. Max van der Stoel, the OSCE High Commissioner on National Minorities, has confirmed that the OSCE has no recommendations with regard to the “*Education Law*”. The Law will become a good tool for promoting social cohesion in Latvia.

The naturalisation procedure

The rate of naturalisation has accelerated considerably after the entry into force of the amendments to the law “*On Citizenship*” in November 1998. As a result, the number of naturalisation applications has increased noticeably, characterised by the fact that in the five months following the entry into force of the amendments the number of applications for naturalisation has more than doubled compared to the number of applications received during the first half of 1998. 8308 persons requested citizenship between November 1998 and May 1999, compared with 2094 applications received in the first six months of 1998. This upward trend continues.

The Naturalisation Board has committed itself to carrying out internal re-organisation to improve the capacity to process the increased number of applications. In April and May 1999 the Government allocated additional funding (37 000 LVL) to the Naturalisation Board with a view to increasing its operational capacities. In case of necessity and with due regard to budget constraints, additional measures to ensure a smooth process of naturalisation will be taken.

The Naturalisation Board has established an Information Centre that will encourage naturalisation and integration of society by improving knowledge about the naturalisation procedure, citizenship requirements and other relevant issues. An information campaign has been initiated in order to improve applicants’ knowledge on naturalisation.

The naturalisation procedure was further streamlined in 1998 and 1999. The naturalisation fee for several groups of applicants has been reduced. Only slightly more than 50% of the applicants pay the full fee. The number of questions for the naturalisation test of Latvian history has been reduced by two thirds (310 questions in 1996, 93 in 1999). More than 95% of applicants successfully pass the tests in the first try.

The progress in the field of naturalisation was confirmed by Mr. Max van der Stoel, the OSCE High Commissioner on National Minorities, who stated in January 1999 that Latvia has fulfilled all his recommendations in the field of naturalisation and that he will not make any new recommendations in this area.

Special passports for non-citizens

By 10 April 1999, more than 66% of Latvia’s permanent non-citizen residents had received special non-citizen passports.

Integration of Minorities

In 1999 a broad public debate on the Framework document of the Integration Programme was conducted. The document had been prepared by a ministerial Integration Council and accepted by the Government in September 1998. In February 1999 the Government set up a Steering group on the development of Society Integration Programme, with the Head of Naturalisation Board as its chairperson. Detailed subprograms and concrete projects of the Society Integration Programme are to be prepared by December 1999. Financial support of 600 000 LVL is provided in the state budget 1999 to implement measures of the Integration Programme such as additional pay for Latvian language and bilingual teachers.

In December 1998, the agreement on the second 2-year phase of the “*National Programme for Latvian Language Training*” was signed. During this phase Latvian language training will be significantly expanded - in the first half of 1999 alone more than 8.500 persons attended Latvian language courses.

In 1998 Latvian language textbooks for specific target groups (e.g. personnel of the Ministry of Interior, Latvian railway personnel, military recruits, etc.) were published. Language courses for vulnerable groups, such as the unemployed, the blind, and the handicapped people, have been offered.

The Latvian Language Training programme enjoys the continuous generous support of the European Commission, which is the largest contributor to Phase II with almost 1 million LVL.

2. Economic criteria

2.1 Introduction

Achieving macroeconomic stability and ensuring economic growth are important tasks for the government in order to promote further sustainable economic growth in the country and thereby diminish the gap between Latvia's economic development and that of the EU. The economic policies of the government are geared towards accession to the EU and provide a positive impetus for economic development, irrespective of the time of accession.

2.2 Economic developments since the Commission published its Regular Report

The macroeconomic situation in Latvia remained stable. Economic growth continued despite a number of external shocks affecting the economy, although at lower rate than was anticipated. The growth in fixed investments and private consumption continued being the principal factors driving economic growth. Domestic lending has increased and foreign direct investment has continuously flowed into Latvia. The Government remains committed towards implementation of prudent fiscal policy and balanced government spending.

Inflation is declining rapidly. Monetary policy in Latvia is mostly focused on maintaining the fixed peg to the Special Drawing Rights basket of currencies. The current account deficit is large, but it is covered by inflows of foreign direct investment (FDI) and long-term borrowing. The recent acceleration in FDI is now related to the restructuring process, especially in the financial sector. The banking sector continues to develop, with a number of internationally respected foreign financial companies having entered the financial sector since mid-1998. The Latvian non-bank financial institutions continue to develop under prudent control of regulatory authorities.

Macroeconomic developments

Real Gross Domestic Product registered very high growth in 1997, at the rate of 8.6%. GDP growth in 1998 was 3.6%. The main reasons for slower economic performance are the demand shocks, which the economy experienced after Russia's economic pressure on Latvia, followed by the full-scale crisis in Russia. However, the ability to withstand and absorb these demand shocks proves in practice that Latvia is firmly on the path of sustainable economic development. Despite these adverse shocks, both the service and industrial sectors have shown positive growth in 1998. The service sector continued booming in the beginning of 1999, accompanied by strong growth in construction. Under the impact of the Russian crisis, the food industry, chemical and machine building have suffered most of all. At the same time production outputs of clothes, ships, wood and wood products and other goods with basic sales markets in the west continues growing. Importantly, construction outputs have risen. Trade also continued booming in the beginning of 1999. On the expenditure side, GDP growth in 1998 was primarily driven by investment, which grew at steady rate of 12%.

The continued inflows in investment have in part been facilitated by improved structural conditions for domestic lending and by the improved legal and regulatory environment of business in the Latvian economy. In particular, the withdrawal of the government as a major borrower from the commercial banking sector has led to a sharp growth in the volume of new bank lending; the overall level of credits to enterprises and households grew by 77.4% in 1997, and a further 49.6% in 1998.

During the last two years, a positive general budget was in place as a result of implementation of strict fiscal policy. In 1997, general government budget surplus reached 1.2% of GDP, and was

0.1% in 1998. The Government continues to implement strict fiscal policy, according to the targets set in the Joint Assessment on Economic Policy Priorities.

At the end of 1998, the total state debt amounted to 9.9% of the GDP compared to respective 12.0% in 1997. Latvia implements a prudent borrowing policy, targeted to shifting the weight from foreign to domestic borrowing in the long run.

The restructuring in government spending policy stressed the necessity to increase public investments. The general level of public investments in 1998 was 2.9% of GDP, compared to 2.6% in 1997. The general level of public investment will reach 3% in the medium term.

Money supply in Latvia continues to grow; in 1998 broad money supply grew by 5,9%. This is in part due to foreign exchange transactions by the Bank of Latvia in order to maintain the currency peg in the face of substantial capital inflows, but also to increased lending by the domestic banking sector. However, due to continued growth in money demand, this has not been a source of inflationary pressure. Moreover, wage dynamics and producer prices have been restrained to date. Inflation has continued to fall rapidly, in average reaching just 4.7% in 1998.

Latvia: Main economic trends		1994	1995	1996	1997	1998
Real GDP growth rate	<i>per cent</i>	0.6	-0.8	3.3	8.6	3.6
Inflation rate						
Annual average	<i>per cent</i>	35.9	25.0	17.6	8.4	4.7
December-on-December	<i>per cent</i>	26.3	23.1	13.1	7.0	2.8
Unemployment rate, end year						
ILO definition	<i>per cent</i>		18.9	18.3	14.4	14.0
Registered	<i>per cent</i>	6.5	6.6	7.2	7.0	9.2
General government budget balance	<i>per cent of GDP</i>	-4.4	-3.4	-1.4	1.2	0.1
Current account balance	<i>per cent of GDP</i>	5.5	-0.4	-5.5	-6.1	-11.0
	<i>billion ECU</i>	0.2	0.0	-0.2	-0.3	-0.6
Foreign debt						
Debt/export ratio	<i>per cent</i>	19.9	19.6	15.8	13.1	12.9
Gross foreign debt	<i>billion ECU</i>	0.3	0.33	0.35	0.34	0.36
Foreign direct investment						
Net inflow according to balance of	<i>per cent of GDP</i>	7.6	5.5	7.4	9.3	4.3
Payment data	<i>million ECU</i>	237.5	198.5	321.4	471	245

Source: Central Statistical Bureau of Latvia, Ministry of Finance of Latvia

*Data from the State Treasury

**ECU=LVL 0.662

The trade and current account deficits of the country remain large, being a matter of increased attention from Latvian authorities. In 1998 the trade and current account deficits for Latvia amounted to 17,6% and 11% of GDP. In 1998 exports grew by 11% and imports by 19% in local currency terms over the same period a year earlier, leading to a further widening of the trade deficit. However, the concerns about the magnitude and medium-term sustainability of current account deficit should not be exaggerated. First, there is no evidence of overvaluation of the national currency. Second, a significant share of the growth of imports is the counterpart of the large FDI and other private long-term capital inflows. The ongoing restructuring of enterprises as well as economic reorientation are considered to be the principal factors in coping with the problem of current account deficit in the medium term.

The official unemployment rate in Latvia has fluctuated around 7% since 1997, although it increased to 9.2% in 1998. However, the unemployment rate measured according to the International Labour Organisation definition gives a different indication of the depth of the unemployment problem in Latvia, and of recent employment creation; it was 14.4% by the end of 1997 and fell to 13.8% in 1998.

The financial and economic crisis, which broke out in Russia in August 1998, had a negative, but manageable impact on Latvian economy. The fall in Latvia's exports to Russia was matched by export growth to its largest trading partner, the European Union, encouraging further trade diversification. While exports to CIS declined by 29.4%, exports to the European Union increased by 27.3% and to other countries by 24.6%. Transit revenues remained at approximately the same level, since Russia continued acknowledging Latvia's comparative advantages in trade in services. Finally, the recent entry of well-known foreign investors, as well as continued favourable ratings by international credit agencies, prove that Latvia is a credible partner for foreign investments.

Structural reforms

The privatisation process is almost complete. 97% of the former state-owned enterprises are now in private hands. By end 1998, 1056 of the 1097 enterprises allocated for privatisation since 1994 had been transferred to majority private ownership. Of the remaining 41 enterprises, privatisation regulations laying out the conditions of sale have been adopted for 18. The privatisation of the three remaining large state enterprises (Latvenergo, Lattелеkom, Latvian Shipping Company) is at the final stage. As a result of privatisation in 1998, pursuant to purchase agreements, the purchasers assumed liabilities in the amount of 23.18 million LVL, and undertook to invest 28.53 million LVL into the purchased asset units. The purchase agreements stipulated retention of 7704 jobs.

The uptake of shares in enterprises by voucher holders has been low. The voucher system is related only to the payment to the state and not to payment to private company shareholders. Vouchers are state-backed securities, and are freely tradable at a market price. More than 100 companies are licensed to trade vouchers. Thus, the investor has easy access to vouchers and the system as such has not caused delays. Secondary markets enabling the trade of small share holdings, and allowing a concentration in ownership, are important in mitigating any negative impact of voucher privatisation. Therefore the voucher system has not led to unclear ownership structures.

In 1997 and 1998, foreign direct investment continued flowing into the country. Much of this improvement can be related to the acceleration of the restructuring process. The largest recipient of FDI has been the transport and communications sector, which has accumulated 31% of the total stock of FDI. The manufacturing and financial sectors are two other major recipients of investment (with 20% and 23% of the total stock). In manufacturing, the processing and chemical sub-sectors attracted most of the foreign direct investment.

In 1997 and first half of 1998, developments in the banking sector continued to be favourable. The situation worsened in the second half of 1998 as a result of the Russian financial crisis. One small bank (*Victoria*) and one medium sized bank (*Kapitalbanka*), whose business was mainly concentrated in Russia, were closed and one larger bank (*Komercbanka*) has been declared insolvent. However, an agreement to re-capitalise the bank was reached among shareholders and creditors of *Rigas Komercbanka* and its rehabilitation began in May 1999.

Despite losses on Russian investments, capitalisation of operating banks remains high – on average 17% capital adequacy ratio at the end of December 1998, based on audited reports. Nevertheless, increased investment as well as entrance of respected foreign banks (*Skandinaviska Enskila Bank*, *MeritaNordBanken*) in the Latvian financial sector ensures its further strengthening and sustainability. The fall in capital base after the Russian financial crisis has ended. Since banks re-valued their investment in Russia and other CIS countries and made additional loan loss provisions, the total equity of credit institutions decreased to 153 million LVL at the end of 1998. Non-performing bank loans by the end of 1998 made up only 7% of the loan portfolio. Moreover,

provisions covered almost all non-performing loans. By April 1999, there were 25 banks and one foreign branch in operation. Further consolidation of the banking sector is expected due to increased capital requirements for credit institutions as of 1 January 2000.

The Bank of Latvia has carried out a thorough assessment of the exposure of Latvian banks both to Russia and other CIS countries. Recognising the high risk of these exposures and aiming to give a clear signal to the market, in September 1998 the Bank of Latvia introduced country exposure limits for Zone B countries at a maximum 25% of own funds of a bank per country and a maximum 200% per total exposure to Zone B countries. Risk weighting of B zone countries' sovereign debt denominated in national currency for the purposes of calculation of capital adequacy ratio was increased from 0% to 50%.

The expansion of the financial sector extends to non-bank financial institutions, especially leasing and insurance companies. The volume of insurance premiums increased by 25,81% in comparison with 1997. The real increase of insurance premiums was 21,11%. In 1998 the share of insurance premiums in the GDP of Latvia was 2,23%.

Due to adverse developments on the Asian and Russian markets, a decline on the Latvian securities market was observed. Share prices and consequently capitalisation of the market lowered. At the same time, the number of listed companies increased from 50 in the beginning of 1998 to 68 by the end of the year. In the medium term, capitalisation will definitely experience a significant growth, since at the moment all shares are substantially undervalued. The other factor to positively impact capitalisation is privatisation of the remaining state shares of the companies, such as Lattelekom, Latvian Shipping Company, Latvenergo, and other enterprises.

In 1998, the total turnover in the securities market was approximately 2.6 billion LVL, which includes the Riga Stock Exchange, over-the-counter market, transactions with government securities and foreign securities. Thirty-four issues with nominal value 126 million LVL were registered in 1998. At the end of 1998, 31 intermediary companies operated in Latvia, of which 13 were brokerage companies and 18 banks.

Considerable progress in Latvian structural policy development has been made in the process of drafting the National Development Plan. At present Latvia is working on many elements of a business and industrial policy in such a way that the government can achieve a coherent policy framework, where different sector strategies are harmonised within the set of agreed priorities. (For more information see chapters *Regional Policy and Cohesion*, and *Industry*)

It is expected that in the nearest future much stronger emphasis will be put on education and training to develop a highly competitive labour force in those sectors where Latvia sees its comparative advantage. The economic development policy will be targeted to increase production of higher value-added goods. Programmes for SMEs, environmental policies, use of innovations and *high-tech* knowledge will be adjusted to follow these trends. Tax policy is still an open issue because of domination of two conflicting positions, where one argues for maintenance of a stable tax regime and the other stresses the need for tax reform to support new business policy developments and decentralisation of government functions to regions and local level.

2.3 Assessment in terms of the Copenhagen criteria

The existence of a functioning market economy

The desire to integrate into the economic and security structures of Western Europe has created a consensus for reform in Latvia. The principal priorities of the new government have not changed and are directed towards the implementation of EU requirements. The consequent implementation

of the National Programme for Integration into the EU continued contributing to an acceleration of reforms in a number of areas. The authorities have made great progress on improving the consistency of economic policy making through the adoption of a medium-term strategy. On 17 February, 1999 the Government and the European Commission signed the Joint Assessment of economic policy priorities, based on medium-term strategy.

Prices for the majority of goods and services in Latvia are freely determined by the interaction of market forces. Only prices for the services of the natural monopolies are regulated. Cost recovery is established, with new payment schedules introduced and the bad debts of the associated enterprises being continuously reduced.

The trade regime in Latvia is very liberal and fully complies with the standards of developed countries. Latvia became a full-fledged member of the World Trade Organisation on 10 February 1999.

To simplify the legal environment the Government submitted to the Saeima the new “*Commercial Law*”, drafted in full compliance with respective EU directives and providing for much more clarity and simplification in the sphere of business activities in Latvia. According to the draft law, the number of forms of enterprises is reduced from the existing 23 to only 5. Furthermore, the number of documents that have to be presented to the authorities for the registration of a company is being reduced and their content and form is aligned with the requirements of EU company law. It is planned to shorten the time period of the registration of a company. The Government is increasingly inviting the business community, both local and foreign representatives, to participate actively in discussions on economic and other policy decisions. These efforts at ongoing dialogue have been noted and appreciated by representatives of the business community.

In order to improve the investment climate in Latvia, the Government commissioned a major report on Administrative Barriers to Investment in Latvia by the Foreign Investment Advisory Service of the World Bank Group. In response to the observations and recommendations of the Report, the Prime Minister established a Working group composed of representatives of the business community and government to elaborate an Action plan on improving the business environment. The Action plan includes more than 40 actions addressing areas of concern for investors, such as simplification of immigration and residence procedures, simplification of customs procedures, establishment of a tax appeals system, streamlining of building permits, development of the land market and rationalisation of government inspections. In all those areas the Working group prepared legal provisions to ensure transparency and consistency in the application of laws and regulations, as well as the public dissemination of information to ensure such transparency and consistency. The Latvian Development Agency is now monitoring the implementation of the Action plan and institutionalising the dialogue between the public and private sectors. Additionally, a meeting of the Foreign Investors’ Council in Latvia in June demonstrated the interest of the foreign investor community in investing in Latvia, as well as the willingness of Government to engage in a high-level constructive dialogue regarding the investment climate in Latvia.

A **bankruptcy mechanism** is in place. Authorities have been taking a number of steps to build a smoothly functioning system to handle bankruptcies. To support the mechanism, in 1995, the compulsory capital requirement was increased over 20 times (from 100 Ls to 2000 Ls). 34,161 enterprises were registered in 1995. Adaptation and implementation of the “*Law on Insolvency of Enterprises*” commenced in 1996. Since 1996, 27,759 enterprises were registered, and in the beginning of 1998, only 237 of them were liquidated. The tendency of stabilisation continues – most of registered enterprises are capable to function and compete in the market.

In October 1998 the Saeima passed the Law “*On Commercial Pledges*” and the respective

Regulations of the Government “*On the Registration of Mortgage Bonds*” were adopted. The most important principle of the Law is the possibility to pledge an enterprise as a going concern.

The **privatisation process** has significantly contributed to the clarification of property rights. The vast majority of the former state-owned enterprises are now in private hands; the private sector accounted for 65% of GDP, and 68% of total employment in 1998. The privatisation of the Savings Bank was completed in 1998. The share of the Government in the banking sector's share capital contracted from 6.8% at the end of 1997 to 4.9% at the end of 1998.

Now only three large companies (more than 500 employees) belong to public sector; they are all in the infrastructure or utilities sectors and completion of their privatisation is planned by the end of 2000. Sectoral strategies for specific areas where privatisation is complicated, such as public utilities, have been elaborated. The recently adopted law “*On the Energy Sector*” allows for restructuring and subsequent privatisation of the Latvian energy company. Only separate objects such as high voltage transmission network are to be kept in state ownership.

In October 1998 the Government took a decision on privatisation of the remaining state shares in *Latt Telekom*. The state share is being decreased in other companies operating in the sector of public utilities. State shares decreased to 39.1% in the Latvian Gas Company and to 43.62% in “*Ventspils Nafta*” (a major oil transit company) in May 1999.

The process of the establishment and evaluation of the legal aspects of an integrated system of **land and property registration** is continuing. In 1998, amendments to the law “*On Land Books*” were passed, providing for the establishment of a computerised system of Land Books. The amendments provide the legal basis for the determination of status of electronic documents and signatures. To ensure the transparency of the registration system, it is planned that the Regulations “*On the Use of information of Public Importance of the Registers for Business Purposes*” will be adopted by the year 2000.

The reform of Land Books carried out in the framework of PHARE technical assistance project will be completed. At the end of 1998, approximately 205 000 (one-third) units were registered in the Land Book. The number is gradually increasing. Land registration in the State Land Cadastre is virtually complete. The land privatisation has been accelerated.

Banks increasingly play the role of financial intermediaries. Prudent financial control makes banks very careful about the quality of loan portfolio. At present the quality of the loan portfolio is fair, with only 2% of bad (lost) loans that are adequately covered by provisions. However, at the end of 1998 credits represented only 15.3% of GDP, and the loan/deposit ratio was 70%.

The Latvian authorities have made considerable progress in establishing the institutions of a market economy. The Competition Council and Competition Board started operation in the beginning of 1998. The State Aid Surveillance Commission effectively performs its duties. The public procurement monitoring system is also being strengthened.

The necessity to strengthen the regulation of public utilities remains an important issue. In April 1999 the Government approved the Concept of the Regulation of Public Utilities. The Concept provides for the establishment of independent regulatory authorities for all kinds of main public utilities, with the gradual merging of these authorities into one joint National Regulatory Authority. Following this concept, the Ministry of Economy has prepared a draft law “*On the Regulation of Public Utilities*” which will act as an umbrella law for the public utility regulation system in Latvia. The government may accept and pass to the Saeima this draft law in 1999. The law could pass all the readings in the Saeima by the end of 1999.

The Russian crisis had a deeper than anticipated, but manageable impact. The economy maintains strong growth prospects. Furthermore, the economic stability has attracted a number of foreign investors. The financing of a high and rising current account deficit is a matter of concern; nevertheless it is fully covered by foreign investments. Foreign trade is being very rapidly reoriented towards the West, boosted by the loss of markets in Russia. The creation of a free market for energy resources, as well as the strategic investor approach significantly reduced Latvia's dependence on Russia for energy imports. Russia's share in Latvia's foreign trade fell (exports 21.0% and imports 15.6% in 1997, compared to exports 12.1% and imports 11.8% at the end 1998), mitigating additional risk for Latvia's external accounts. On the other hand, Latvia continues to benefit from transit trade from Russia, and strong positive trends are being observed in this direction.

Latvia is making continuous and steady progress in its programme of economic reforms and in the creation of a functioning market economy. Many important reforms have been implemented and appear to be efficient. Latvia has succeeded in filling up the remaining gaps in the regulatory and supervisory framework, as well as in the financial sector and simplification of the legal environment for enterprises.

The capacity to cope with competitive pressure and market forces

A detailed plan for meeting the criterion is being incorporated in the updated III National Programme for Integration into the EU, the Medium term Economic Strategy in the Context of Accession to the EU, as well as the Joint Assessment of Economic Policy Priorities of Latvia. These documents provide a stable framework for pursuing consistent market oriented policies aimed at further strengthening of the market economy and enhancing the ability to withstand competitive pressure within the internal market.

As a result of sustainable and consistent implementation of reforms, Latvia can now be considered a fully functioning market economy. This has contributed significantly towards improvement of Latvia's prospects for developing the capacity to cope with competitive pressures within the single market. Enterprise privatisation and restructuring have led to a more flexible enterprise sector, which is more responsive to market conditions.

Sound government policies have resulted in increasing macroeconomic stability and more consistent macroeconomic direction. These have contributed to strengthening an environment more conducive to domestic investment, as well as attracting higher levels of foreign direct investment. Investment as a share of GDP continues to grow.

The privatisation process is an important step in preparing the Latvian economy for competitive pressures within the internal market. At present, progress has been made in stipulating enterprise restructuring. The government has launched a comprehensive SME development programme, one pillar of which is the establishment of the Latvian Guarantee Agency to provide guarantees for loans to SMEs (For more information see *Small and Medium Enterprises*).

Authorities have made great strides in introducing and implementing EU quality standards to ensure competitiveness of producers in domestic and foreign markets. At present, approximately 300 EU standards have been adopted as Latvian national standards. The full implementation of EU standards will be ensured by the end of 2002, as provided by the respective programme. Many companies are in the process of adjusting their business to EN 29001-3 standards.

Latvia has a relatively well educated labour force. Generalised education indicators of the workforce (November 1998) are as follows: higher education – 19.5%; specialised secondary (professional post-secondary, non-tertiary, level 4 by ISCED 1997) or upper secondary

professional education – 48.1%; and general upper-secondary education – 24.1%.

The need for reforms in the restructuring of labour capital have already led to the following: 16600 (14.9%) officially unemployed persons have passed re-qualification courses, 37.8% succeed in finding work. 11700 (12%) unemployed persons have started re-training courses. 600 re-training programmes are available, ensuring 100 new specialities.

The promotion of **infrastructure investment** is an important priority. The government has significantly increased budgeting for higher investment spending, and a high level of government spending on infrastructure is expected in the medium term. The Government's state investment policy is realised through the Public Investment Programme, which includes significant infrastructure development projects. State basic budget investments increased from 0.7% of GDP in 1997 to 1.3% of GDP in 1999. State budget investments are also co-financing for EU ISPA projects through Public Investment Programme.

The structure of the Latvian economy has continued to evolve towards the model known in the more advanced industrialised economies. In particular, the agricultural sector is declining in relative importance, and the service sector accounts for a larger share of output. The service sector has been one of the most dynamic parts of the Latvian economy in recent years, and constitutes an important share of exports (around 31%). In this respect, Latvia benefits both from its unique geographical location as a transit route between East and West, and the good infrastructure of its ports, railway lines and pipelines. This is an important source of competitiveness for the Latvian economy. Moreover, both the ports themselves and the transport routes servicing these ports are being upgraded.

Restructuring of the agricultural sector and rural economy is one of the most important challenges for Latvia's economy. Agricultural employment is still considerably high at 15.7 % (1998) of the total workforce, whilst farm efficiency is comparatively low. It is expected that agricultural output will continue to decline against the GDP during the coming decade and agricultural employment will decrease. To modernise farm production and diversify rural economy, new policy initiatives have been taken. The Agricultural Development Programme was adopted in autumn 1998. Support (direct subsidies) for agriculture and rural development has been increased up to 3% from the state budget. A Rural development plan is currently being drafted, envisaging co-financing from the SAPARD fund and national budget. The main priorities under SAPARD measures will be farm investment, modernisation of food processing and marketing, rural diversification, environmental measures, improvement of rural infrastructure and training.

Exports are growing consistently faster than GDP. In 1998 exports flows grew by 10% despite a continuous real appreciation of the national currency with respect to the western currencies. The degree of trade integration with the EU increased. During the first three months of 1999, exports and imports to the EU comprised 64.9% and 55.7% of total exports/imports respectively.

The share of processing industries in total exports remains dominant at 89.8%. In 1998, the biggest increase in export was noted in the following products of the processing industry: wood and articles of wood (18.9%), textiles (8.8%) and products of chemical and allied industries (5.5%).

10% of all investment in the manufacturing sector goes to the wood-processing sector. This has led to an increase in value added of the products of wood. The quality of Latvia's wood production is supported by the fact the UK has switched its wood imports from traditional partners (Finland, Sweden) to Latvia. Presently Latvia is the second largest wood exporter to the UK.

Integration of the financial markets of the Baltic States is continuing. The integration of the

securities markets of the Baltic States in the short term and then their integration into the European securities market in the longer is one of the top policy priorities. This will ensure so-called economies of scale. The Baltic States Securities Market Supervisory institutions cooperate with the goal of promoting and developing a unified Baltic securities market. The authorities of the Baltic States have signed an agreement on information exchange. The Baltic States Securities Market Supervisory institutions also work towards developing a unified licensing and registering procedure for all three Baltic States. The Riga Stock Exchange is actively working towards developing and establishing a unified Baltic Stock Exchange. In April 1999, the Riga Stock Exchange signed a Protocol of Intent with Tallinn Stock Exchange and Vilnius Stock Exchange.

Most of the conditions necessary for the acceleration of restructuring in Latvia's economy, which would lead to sustained increases in competitiveness, are now in place. Much has been done to achieve sustainable macroeconomic stability and to implement the reforms needed to create a market economy. Investment in Latvia has increased, and privatisation is completed in principle. Latvia has succeeded in maintaining macroeconomic stability, and ongoing sustained progress with the reform programme enables Latvia to cope with competitive pressures and market forces within the Union in the medium term.

3. Ability to assume the obligations of Membership

3.1 Internal Market without frontiers

General framework

The Europe Agreement provides guidelines for gradual implementation of the four freedoms and approximation of legislation. The political and administrative system of Latvia has proved effective in executing tasks in accordance with the Third National Programme for Adoption of the *acquis*, and the simultaneous work on EU and Latvia's legislation has ensured a consistently up-to-date set of legislative acts.

In 1998, Latvia made further progress in implementation of EU framework directives concerning regulation of a market economy.

Tight control of compliance with the rules of public procurement is one of the top priorities of the Government. Extensive work has been done in the area of educating procuring entities. The EU provided significant assistance in this area. In December 1998 the Saeima adopted in the first reading the "*Law on Works, Supplies, Lease and Services Procured by Entities operating in the Public Utilities Sector*". This is a noteworthy step forward to full transposition of the EU requirements in the area of public procurement. Pursuant to the terms of its accession to the WTO, Latvia has prepared a draft application for joining the WTO Government Procurement Agreement.

The "*Law on Joining the Rome Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organisations*" is in force since October 1998.

It is expected that Latvia will join the WIPO Copyright Treaty and WIPO Performances and Phonograms Treaty by the end of 1999. The draft law on joining the WIPO Copyright Treaty and WIPO Performances and Phonograms Treaty is currently being prepared.

On 10 February 1999 Latvia became member of WTO and joined the TRIPS agreement.

On 1 July 1999 the regulation "*On Customs Control Measures for Protection of Intellectual Property*" comes into force.

In October 1998 Latvia adopted Amendments to the "*Administrative Offences Code*" on illegal distribution of neighbouring rights to a work and the use of copyrighted work without a licence.

Latvia has already acceded to following international agreements in the field of industrial property protection:

- *The Paris Convention for the Protection of Industrial Property;*
- *Patent Co-operation Treaty;*
- *Madrid Agreement Concerning the International Registration of Marks;*
- *Budapest Treaty on the International Recognition of the Deposit of Microorganisms of the Purposes of Patent Procedure;*
- *Nice Agreement Concerning the International Classification of Goods and Services for the Purposes of the Registration of Marks.*

The Saeima is expected shortly to approve Latvia's accession to the *Trademark Law Treaty* and the *Protocol relating to the Madrid Agreement*. The Saeima will also pass a new law "*On Trademarks and Geographical Indications*".

The new Criminal Code (in force since April 1999) contains provisions of criminal responsibility for infringement of copyright and illegal use of copyrighted work and neighbouring rights.

In the area of accounting the greatest attention is being paid to:

- Transposition of the Consolidated Accounts Directive. In January 1999 the Government accepted the draft law “*On Consolidated Accounts*”. Being compliant with the 7th EU Directive, the bill is expected to be adopted by Parliament in 1999.
- Revision of the law “*On Sworn Auditors*”, raising requirements for the educational level of sworn auditors and strengthening supervision thereof. Such amendments to the law “*On Sworn Auditors*” will be submitted to the Government by the end of 1999. Amendments bringing the law in closer compliance with the respective EU directives are being elaborated with the goal of being adopted by mid-2000.

The law “*On Protection of Personal Data*” was adopted in the first reading by the Saeima on 16 October 1998.

The Four Freedoms

Free Movement of Goods

Since October 1998 the horizontal legislation in the field of free movement of goods is in place. Progress has been achieved in harmonisation of the sectoral legislation. All quantitative import restrictions have been eliminated. It is expected that most of the legislation related to the free movement of goods will be adopted by the end of 1999. As mentioned in the introduction, negotiations on a Protocol on Conformity Assessment have begun.

The overall framework of the conformity assessment legislation is defined in the law “*On Conformity Assessment*”, which is now being aligned according to the recommendations of the European Commission. Amendments to this Law will be enforced by the end of this year.

A new law “*On Standardisation*” was passed in October 1998. According to the Standardisation Development Programme more than 350 European standards in the different fields have been adopted so far and the programme focuses on the acceleration of the process of implementation. All European standards will be adopted before the end of 2004.

The National standardisation institution has been reorganised. The status of the “*Latvian Standard*” Ltd ensures its independence from the administration.

The accreditation body LATAK (Latvian National Bureau of Accreditation) is an affiliate member of the European Co-operation for Accreditation (EA) since January 1999. In accordance with European EN 45 000 series standards, LATAK has accredited 84 testing laboratories in different areas, 1 personnel certification body, 3 product certification institutions, 3 calibration laboratories, 5 inspections and 1 quality systems certification body.

The concept of a market surveillance system is being elaborated and will cover a general - horizontal market surveillance system for consumer protection from unfair presentation, packaging, marketing and marking for products and a vertical system in sectors for evaluation of the frauds caused by different unsafe products in the market.

Progress has been made relating to the implementation of new approach directives. Essential requirements of the directives on electrical safety and electromagnetic compatibility of apparatus have been incorporated into two regulations of the Government of April and May 1998. The Regulation on the Conformity Assessment for Construction Products of August 1997 fully corresponds to the requirements of the EU. The Regulation On Personal Protective Equipment

and the Regulation On Simple Pressure Vessels, compatible with relevant EC directives, were adopted in December 1998 and March 1999. The Regulation On appliances burning gaseous fuels will be adopted in the second half of 1999. The Regulation On Machinery Safety, Regulation On Pressure Vessels and Regulation On Equipment and protective systems intended for use in potentially explosive atmospheres will be adopted in the 3rd quarter of 1999. These regulations implement the requirements of the corresponding directives.

In the field of Type Approval of motor vehicles, the Regulation On Conformity Assessment of Wheeled Vehicles and their Components was adopted in March 1999. On the basis of this regulation, the Ministry of Transport will issue secondary legislation which will transpose the requirements of separate directives.

Most of the requirements of directives concerning foodstuffs have been implemented. The Law *“On the Surveillance of Food Circulation”*, adopted in February 1998, provides for the implementation of EU directives concerning food control and food hygiene. Several regulations of the Government have been accepted in areas such as products and articles coming into contact with foodstuffs, hygiene of fishery products, hygiene of food enterprises, solvents for use in food production, veterinary requirements for slaughtering of animals, control of radioactive contamination, and labelling of foodstuffs. It is planned to adopt regulations on contaminants of food, on novel (genetically modified) food and novel food ingredients, as well as regulation on honey, on fruit jams, jellies, marmalades and chestnut puree and on fast foods by the end of 1999.

The new law *“On Chemical Substances and Chemical Products”* was adopted in April 1998. According to this law, the Government has approved the Regulation *“On the Security Data Sheets”*. The following regulations will be adopted by the October 1999: *“On the Classification, Packaging and Labelling of Chemical Substances and Chemical Products”*; *“On the Limitation of the Use and Trade of Dangerous Chemical Substances and Dangerous Chemical Products”*;

A law *“On Pharmaceutical Activities”* incorporates the relevant provisions of EU legislation. The regulations *“On the Registration of Medicinal Products”*; *“On Classification of Medicinal Products for Human Use”*; *“On the Labelling of Medicinal Products and Package Leaflets”*; *“On reimbursement of medicinal products for ambulatory care”* have been adopted.

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

Free Movement of Capital

Latvia has a liberal regime for capital movements that may well be compared to the world's most liberal regimes. No restrictions on convertibility of national currency exist in Latvia both in respect to the current account and capital account transactions. Foreign investors can freely repatriate their investments and profits after paying due taxes. Both residents and non-residents are allowed to hold foreign currency in cash or open bank accounts in the Latvian or foreign currency without any restrictions. Every Latvian resident may use foreign financial services without any restrictions.

Currently, restrictions on FDI inflow in Latvia remain only in 4 branches of the economy - logging business, radio and TV, security and lottery and gambling business. FDI in the aforementioned sectors is not completely prohibited. Non-residents may own up to 49% (50%) in the companies in these sectors. In the logging sector it is foreseen to revise these restrictions in 1999.

As to the restrictions for Latvian companies to invest abroad, currently these exist for prudential reasons only in respect to private pension funds: these cannot invest abroad more than 15% of the

total value of pension fund assets as well as for the Deposit Guarantee Fund, which is to invest solely in Latvian government securities.

No restrictions are applicable to transactions in securities. No restrictions exist for the purchase of buildings.

Major liberalisation of the regime of foreign investment in the land market was carried out in 1996-1997. Nevertheless, it was realised that additional liberalisation measures would be necessary for further improvement of the business climate. Therefore, the respective laws (*law "On Land Reform in Cities of Latvia"* and *law "On Land Privatisation in Rural Areas"*) are being currently revised.

Firstly, the prohibition of purchase of land in certain territories (land near the border of the state, in environmentally protected areas, around water reservoirs; land earmarked for use in agriculture and forestry in the general development plan of the territorial unit) by the companies where control belongs to the states with which Latvia has no agreements on promotion of investments (exception is public joint stock companies, shares of which are quoted on the stock exchange) will be revised.

Secondly, it is planned to alleviate the authorisation process for purchase of other land by the aforementioned companies.

Free Movement of Services

In recent years, so much effort has gone into perfecting the legislative basis of financial services that further development of that industry mostly depends on successful implementation in this sector.

The Saeima passed amendments to the Law "On Credit Institutions" in May 1998, setting improved procedures for bankruptcy, liquidation and rehabilitation of credit institutions. The aforementioned amendments also establish a legal basis for the introduction of consolidated supervision. The Bank of Latvia approved the necessary implementing rules in March 1999. In addition, the amendments to the Law enable the supervisory authority to exchange information required for implementation of consolidated supervision with other supervisory institutions, both domestic and foreign. The Bank of Latvia has also approved the necessary regulations to implement consolidation requirements in respect to annual accounts of the credit institutions, thus fully implementing the EU Directive on Annual Accounts and Consolidated Accounts of Banks and other Financial Institutions. The new provisions will be applicable to year 1999 annual accounts of banks.

The Bank of Latvia has implemented all first stage measures in respect to banking supervision prescribed by the White Paper, and part of second stage directives, such as the Second Banking Directive, the Large Exposures Directive and partly the Directive on Annual Accounts and Consolidated Accounts of Banks and other Financial Institutions, and the Directive on the Supervision of Credit Institutions on a Consolidated Basis.

It should be emphasised that the provisions of some of the introduced regulations are even tighter than the EU requirements and they already being implemented. Full implementation of the Capital Adequacy directive and the adoption of the regulations on capital adequacy requirements for investment companies and Regulations of the Bank of Latvia on capital adequacy requirements for credit institutions is scheduled for the year 2000. A joint Task Force has been formed consisting of the representatives of the Bank of Latvia and the Securities Market Commission to ensure transposition of CAD Directives and to work out a uniform approach to trading activities

both of credit institutions and investment firms, thus avoiding contradictions. EU consultants are assisting the task force in the framework of the PHARE project.

In the securities area, the most important event in 1998 was implementation of the Directive on the co-ordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities. The respective law "*On investment companies*" comes into force on 1 July 1999. The Securities Market Commission approved a full package of by-laws for smooth functioning of the investment companies: Regulations "*On Auditors of Investment Funds*"; Regulations "*On Licensing Investment Companies*"; Regulations "*On Accounting and Financial Statements of Investment Funds*"; Regulations "*On the Distribution of Investment Certificates or Securities of Foreign Funds in the Republic of Latvia*"; Regulations "*On Requirements Concerning Liquidity and Other Financial Indicators of Investment Companies*". After adopting the aforementioned legal acts, two investment companies were licensed.

Furthermore, the Securities Market Commission initiated quite a large number of amendments in the standard securities market regulatory framework (in law "*On Securities*" and other normative acts in respective field), the necessity of which was realised while performing supervisory activities.

During 1998, the Council of the Securities Market Commission passed several amendments to the laws and regulations designed to promote further securities market development, improve public disclosure, and enforce further harmonisation with EU directives. The most substantial amendments are contained in:

- Order "*On the Preparation of Reports on Securities Transactions*"
- Regulations "*On Registering Securities and Receiving Authorisation for Public Issues of Securities or Releasing Securities for Public Circulation*"
- Regulations "*On Disclosure of Issuer's Material Events*"
- Regulations "*On Registering Securities of Public Properties under Privatisation and Receiving Authorisation for their Public Trading*"
- Regulations "*On the Issue of Licenses for Activities of Professional Specialists on Securities Market*".

The amendments to the previously adopted law "*On Securities Market Commission*" enhanced the Securities Market Commission's powers in areas such as administrative investigation activities and the performance of audits and control functions.

On 10 September 1998, the Saeima adopted the law "*On Mortgage-Backed Securities*". Now it is legally possible to introduce a new kind of financial instrument in the securities market. According to the aforementioned law, on 26 June 261998, the Securities Market Commission passed the Regulations "*On Collateral Register of Mortgage Bonds*". As to future actions to complete transposition of *acquis* requirements, apart from introduction of requirements of the Capital Adequacy Directive, scheduled for mid- 2000, it is also planned to introduce an investor guarantee scheme (possibly from 1 January 2001) and the preparatory work will be started already in 1999.

On 1 September 1998, new laws in the insurance field - the law "*On Insurance Contract*" dealing with private law norms, and the law "*On Insurance Companies And their Supervision*" dealing with public law norms, came into force. As a result, major non-compliance with EU requirements was removed.

The insurance supervision inspection adopted all necessary implementing regulations to ensure correct application of the norms stipulated by the new laws - Regulations of the Cabinet of

Ministers “*On Administration of Resources of Insured Protection Fund*”; “*On Order of Certification of Insurance Brokers*”; “*On Civil Liability Insurance of Insurance Brokers*”; “*On Order Of Making Payments to Insured Protection Fund*”; “*Registration Order of the Insurance Intermediaries Services for Companies of Insurance Brokers*”; “*Rules of Registration for Insurance Agents and Agency*”; and “*On Formation of Annual Accounts of Insurance Companies*”.

The Traffic Bureau of Latvia was admitted to the Green Card System as a “Transitional Member” with effect from 1 July 1998. Latvian Green Cards came into circulation from 1 December 1998. In February 1999 the Government approved amendments to the regulations “*On amount of Premiums and insurers' Liability Limits in Mandatory insurance of Civil Liability of Transport Vehicle Owners*”, whereby insurers' liability limits were doubled. The present amount of guarantees covers the average claim volume in Latvia. The limits will be periodically revised, but it is difficult to foresee now when the guarantee amounts will reach the minimum requirements of EU.

A key element in the supervision strategy of the financial market is the establishment of a single financial market (banking, insurance and securities market) supervision authority. The idea of establishing this institution was supported by the Government on 20 June 1998, and this is considered to be an irreversible process. The draft “*Law on Consolidated Supervision of Financial Sector*” is to be prepared in 1999.

Free Movement of Persons

(a) Free Movement of Union Citizens; Freedom of establishment and Mutual Recognition of Diplomas and Qualifications

The draft law “*On Regulated Professions and Recognition of Professional Qualifications*”, comprising fundamental norms in the field of mutual recognition of professional qualifications included in the Treaty, and more than 50 directives were considered and accepted in the Committee of the Cabinet of Ministers on 14 June 1999.

Co-ordination in the field of social security is fostered by bilateral agreements. An agreement on social security with Finland was signed on 11 May 1999.

For improving and simplifying the process of regulation of free movement of labour force within the Baltic States, Latvia and Lithuania are drafting an Agreement On free movement of workers within the Baltic States. The Agreement is elaborated on the basis of European Union legislation.

(b) Abolition of checks on persons at internal frontiers

Specification of a joint visa information system has been elaborated. It is expected that the system will become operational by January 2000.

Since September 1998 bilateral visa-free regimes have entered into force between Latvia and Austria, France, Greece, Croatia, Italy, Slovenia, Spain, Germany and Portugal and have been signed with the Benelux states.

In order to improve security of citizens' passports, a tender for the design of the new passport was held. The results of the tender have been submitted to the Government.

Since September 1998 Latvia has concluded agreements with Greece, Croatia, Slovenia, Spain and Germany on the readmission of persons residing illegally.

Competition

The goal of the competition policy of the Government is to ensure equal conditions for all market participants.

In 1998 the work on improvement of the legal framework continued. Secondary legislation in the anti-trust area is being improved and developed in line with the National Programme for Integration into the European Union and the "*Competition Law*".

The new "*Competition Law*", already in force for a year, is effective and in conformity with EU requirements. On September 1998, Government passed regulations on Agreements "*On Production Specialisation exempt from Agreement Prohibition of the Competition Law*".

The Government has issued several regulations, which set four groups of agreements which are exempted from prohibition by the "*Competition Law*": exclusive supply agreements and exclusive purchase agreements, agreements on production specialisation, franchise agreements, agreements on joint research and development, licence agreements on patents and know-how, vehicle distribution agreements, as well as on agreements between insurance companies. It is planned to adopt regulations of the Government on the application of "*Competition Law*" provisions in the sphere of transport and to prepare amendments based on implementing practice of several existing regulations during the year 1999. To facilitate implementation of regulations of the Government, the Competition Council has approved and published methodical guidelines on how to compile notifications of collusion and statements of merger.

During 1998 the Competition Council reviewed seventy-six cases. Twenty three of them were linked with abuse of authority, 15 - prohibited agreements, 7 - mergers, 24 - unfair competition and misleading advertisement, 7 - other.

Latvia has a fully functioning and consistent state aid control system. The appropriate legislation has been in force for more than a year. The independent State Aid Surveillance Commission has adopted decisions on eight state aid projects. Latvia fulfils its obligation stemming from the Europe Agreement in respect to transparency in state aid matters. The decisions of the State Aid Surveillance Commission are public. Comprehensive information on aids granted under all existing state aid programmes and individual state aid projects are presented in regular reports produced by the State Aid Surveillance Commission. The new state aid projects (submitted after establishment of the legal framework for control over state aids) are also registered in a special electronic programme. In 1999 it will be possible for the first time to obtain information about the corporate income tax discounts (1998 data) that were made available to microenterprises and companies that have foreign capital. For the first time there will also be complete information about state aid that has to do with tax extension with respect to taxes that are to be paid into the national budget.

In March 1999 the Government approved the new concept paper on the regulation of public utilities, according to which the new law will be drafted. In broad lines it follows the idea that the regulation of the public utilities sector is an important element of the overall development of the state's economy and it should serve the public interests. It is planned that the regulatory authorities will consist of decision-making and executive institutions, which will be formed of highly professional personnel. The draft law "*On the Regulation of Public Utilities*" will be prepared this year.

3.2. Innovation

Information Society

Latvia is actively pursuing modernisation and establishment of the legal framework for information and communication technologies. In order to promote an information society, the Ministry of Transport began implementing the Latvian National Programme “*Informatics*” (Action plan for years 1999-2005). In March 1999 it was presented to the EU/CEEC Joint High Level Committee on Information Society.

The law “*On Access to Information*” was accepted in November 1998 and the law “*On Protection of Personal Data*” was passed to the first reading in the Saeima in October 1998. During this year Latvia also plans to adopt the law “*On State Information System*”, as well as to join the Council of Europe Convention on Protection of Individuals with regard to Automatic Processing of Personal Data.

The establishment of an education informatisation system in Latvian schools, begun in 1998, continued this year, during which creation of regional support centres was carried out. Centralised resources for user training are being developed and 170 teacher trainers have been prepared for the regional support centres, which trained more than 600 teachers in 1998. 1998 was also the second year of development of the Latvian Library Network.

The legislation in force foresees that by 2003 all general and professional educational facilities in Latvia will offer a computer class and provide a common network and access to the Internet. There were approximately 100 000 Internet users in Latvia at the end of 1998 and the number of Internet hosts exceeded 13 000.

In 1998 the pilot stage of the Baltic Government Data Transmission Network was implemented and the Latvian Enterprise Register and the State Vehicles Register are prepared to join the corresponding European Business Register (EBR) and EuCaris system. These projects should be viewed as a practical step towards co-operation under the EC IDA Programme (Interchange of Data between Administrations). The first phase of the Project of Integrated IS of registers of national importance (Megasytem) was worked out in 1998. The development of this Project is connected with the implementation of the Complex State Revenue Service IS.

In total, 16 million LVL are to be invested in the public IT&T sector during 1999.

Education, Training and Youth

The Strategic programme on development of education “*Education 1998-2009*” was adopted in 1998. State budget expenditure for education was increased by 6.4 % in 1999 in comparison with 1998. A crediting system for financial support of tertiary students was established in 1998. The number of students increased by 18% in 1998 in comparison to 1997, reaching a total of 76653 students.

A new framework “*Education Law*” was adopted in October 1998. Thus, EU requirements on education of children of migrant workers have been fully transposed. In 1999 drafts of a “*General Education Law*” and a “*Vocational Education Law*” will be adopted by the Saeima. These laws provide transition to an education programme principle and introduce the concept of national curriculum standards for all stages and types of education.

On 6 May 1999, the World Bank approved a loan of 18.3 million LVL for the Education Improvement Project. The project’s objectives are to improve energy efficiency and space

utilisation of the first 116 educational facilities and to build and strengthen institutional management capacity to assess and promote quality of learning.

Latvia is undertaking reform in the vocational education and training (VET) system to enhance the readiness of Latvian society to cope with the demands of a modern and dynamic labour market. The reforms are establishing a qualitative, accessible and flexible VET system in Latvia, including the introduction of regional training networks/consortia. EU PHARE has provided substantial support for these reforms. In addition, work has started on the improvement and decentralisation of the VET management and financing system.

Since November 1998 Latvia is participating in the SOCRATES, LEONARDO DA VINCI and Youth for Europe programmes. An agency for Youth international programmes as national co-ordination unit was established in April 1999.

The Higher Education Evaluation Centre is offering activities related to quality assurance in higher education. In total, 30 study programmes were accredited by April 1999. The Academic Information Centre carries out the academic recognition of foreign qualification and provides information to EU Member States and associated states within the EU NARIC network and within the joint Council of Europe/UNESCO ENIC network both in terms of the SOCRATES programme and beyond it.

Research and Technological Development

The priority research directions are (1) information technology and telematics; (2) organic chemistry, biomedicine and pharmacy; (3) new materials and technologies; (4) forestry and wood sciences.

The government has charged the Ministry of Education and Science with the draft of the “*State innovation policy*” for arranging innovation activities in Latvia and developing competitive production of high value-added goods.

Two universities and several scientific institutions have participated in 65 research projects within the EU 4th Framework programme for Research and Technological Development. In the last call for proposals of the 4th Framework Programme, 22 projects of Latvian researchers have been confirmed for funding.

Latvia had official negotiations for full association with the 5th Framework Programme in autumn 1998. The draft decision of the Association Council has been prepared, and a draft law “*On Participation of Latvia in 5th Framework Programme*” has been submitted to the Government. It is anticipated that the Saeima will pass the law by end of September 1999.

The PHARE programme in 1998 provides 94 000 LVL for the project “*Investment support for participation in the EU RTD programmes*”.

A National Contact Point was created in March 1999 with the aim to co-ordinate the activities in all thematic and horizontal programmes, to provide potential participants with required information, to help in partner search and to draw up the project proposals.

Telecommunications

Latvia’s telecommunication sector progressed remarkably. Modernisation of the fixed network is ongoing. At the end of 1998 the number of main lines, including extensions in the fixed network, reached 820000. There are already 40% digital lines and 60% analogue lines. Competition between two cellular operators has led to a rapid increase in mobile penetration and extended

coverage in the last two years. The first Interconnection Agreement between *Lattelekom* and Latvian Mobile Phone was concluded in February 1999. At the end of 1998 mobile penetration was 6,1%.

In October 1998 the Government decided to privatise the remaining state shares in *Lattelekom*. In 1998 the Government adopted a Telecommunications sector policy for the period 1998 - 2003 and undertook commitments to restructure the sector in order to ensure the end of the exclusive rights of TILTS Communications. At present, the Latvian Privatisation Agency, responsible for the state shares in *Lattelekom*, is negotiating with 'TILTS Communications' on the compensation for the monopoly reduction.

The draft "*Telecommunications Law*" will be submitted to the Saeima in September 1999, and will be adopted by the Saeima before the end of 1999. It will provide for the establishment of a new regulatory institution, an independent National Telecommunications Regulator. Provisions for Universal Service, Open Network Provision and other provisions in accordance with EU Directives are set out in this law.

All ETSI (European Telecommunication Standardisation Institute) standards are gradually being adopted since November 1998, when the Ministry of Transport became a Member of ETSI. The Department of Communications of the Ministry of Transport and Telecommunication Tariff Council currently fulfils a part of the functions of the NRA (National Regulatory Authority). An application for Membership of CENELEC (European Electrotechnical Standards Committee) was submitted in January 1999.

Lattelekom plans to invest 60 million LVL in development in 1999.

Audio-visual

The audio-visual sector in Latvia is characterised by rapid growth. Its ability to adhere to the acquis presupposes an upgrading of the capacity of the programme-making industry to meet the important challenges of an adapted regulatory framework.

The law "*On Radio and Television*" is in broad terms harmonised with the Television Without Frontiers Directive, including European norms on the proportion of European works and of works produced in the Latvian language, on the proportion of independent producers and on the freedom of reception, as well as on the advertising, sponsoring and protection of minors. The amendments aligning the "*Radio and Television Law*" with the Directive entered into force in November 1998. The European Commission has pointed out some further differences in the Law. Further minor improvements of the Law "*On Radio and Television*" are in progress.

Latvia intends to join the Media II programme, and in co-operation with other European countries to develop the intellectual and production output of the industry. This will be possible after the completion of the harmonisation of Law "*On Radio and Television*" with the Directive.

The Council of Europe Convention on Transfrontier Television was ratified in May 1998.

The independent regulatory body under the Law is the National Radio and Television Council (NRTVC), whose main objectives are to issue broadcasting licences and monitor observance of the law.

3.3 Economic and Fiscal Affairs

Economic and Monetary Union

Latvian authorities have a clear-cut policy on the EMU: Latvia must be able to join the European Monetary Union at the time of its accession to the EU. The Government and Bank of Latvia have adopted macroeconomic policies designed to strengthen stability, which are compatible with the principles of the EMU.

The operation standards of the Bank of Latvia mostly comply with those of the European Central Bank. Latvia already complies with two Maastricht convergence criteria - on budget deficit and foreign debt. In principle the currency stability criterion is also observed, as the lat is pegged to SDR since 1994. The inflation rate is also very close to Maastricht standards.

The law "*On the Bank of Latvia*" was recently amended to prohibit granting of short term credits to the government by the Central Bank. In fact, such borrowing has not taken place for the last 3 years. The Government will continue to implement a strict fiscal policy, by ensuring a financially balanced state basic budget. The fiscal deficit will be managed within the defined limits of the Maastricht Treaty. The currency peg will be maintained.

Presently the Bank of Latvia is preparing introduction of the real time gross settlement system. It is expected that the system will be introduced by the year 2001.

Taxation

From the very beginning of transition, Latvia has been paying close attention to reorientation of the tax system towards the principles of the market economy. At the moment, the Latvian **tax system** generally complies with EU regulations. The transposition of the main requirements of the EU normative basis on taxation was completed at the end of 1998.

In 1998 and the beginning of 1999, thorough work has been done to reduce the remaining deviations. As a result, amendments to the law "*On Value Added Tax*" were adopted, stipulating: (1) abolition of VAT exemptions for mass media from 2002, as well as (2) introduction of special norms of application of VAT to transactions with timber aimed at improvement of administration thereof along with prevention of unfair competition in the wood logging, processing and export business. New legislation also envisages that repayment of VAT for foreign natural persons will commence at the beginning of 2000. In the medium term, the Latvian authorities will focus on the remaining exemptions from VAT (i.e. gradual cancellation of the exemptions not provided for in EU legislation). For the time being, Latvian legislation does not provide for repayment of VAT for foreign legal persons. In the majority of countries this system functions according to the principle of mutuality and is based on exchange of information. The system is expected to be introduced in Latvia by 2003.

In order to harmonise the excise tax system, new excise duty laws concerning alcoholic beverages and tobacco articles came into force from 1 January 1999. For the time being, the law "*On Excise Duty on Tobacco Articles*" sets a lower excise duty rate on cigarettes than that determined by the relevant EU Directives. It is envisaged to establish excise duty rates on tobacco articles in accordance with the minimum level set out by the European Union by 2003.

The law "*On Excise Duty on Alcoholic Beverages*" is a further step towards approximation of the Latvian system of excise duty with EU requirements. It should be noted that excise duty rates for alcoholic beverages already now exceed the minimum level set out by the European Union. For the time being, in Latvia excise duty is levied only on beer with an alcohol percentage of 5,5 and

upwards. The law “*On Excise Duty on Beer*” will be drafted by September 1999 to remove this non-compliance.

Great progress has been achieved in strengthening administrative capacity in the area of tax and customs administration since establishment of the State Revenue Service.

To streamline the process of upgrading the State Revenue Service, a **comprehensive SRS modernisation programme** (1998 - 2002) was elaborated in collaboration with the World Bank. Sufficient resources are provided by the national budget and international donors for successful implementation of the SRS Modernisation Project.

Among the latest noteworthy achievements are the following:

- technical equipment corresponding to requirements of the new tax administration system was ensured;
- regular exchange of information between the tax system and the Residents and Enterprise registers was assured;
- 18 regional divisions of the State Revenue Service were linked to the unified global computer net;
- a new tax payers’ register was introduced and is already in use in SRS headquarters and all regional divisions;;
- personalised accounting of social contributions was started;
- the methodology of tax debt recovery was improved;
- the Tax audit manual was supplemented with issues related to audit of separate taxes; an agreement on simultaneous audit in the Baltic States was prepared; instructions on simultaneous inter-state audit were drafted;
- the necessary regulations on financial stimulation of SRS personnel, on evaluation of results of work of SRS staff, on selection of SRS personnel, etc were adopted.

Serious preparatory work is being done for introduction of a 3-level tax administration system (this is one of the largest projects of the SRS modernisation programme). As a major practical step towards establishment of this system, on 22 April 1999 two new pilot Regional SRS Institutions commenced optimisation of the respective SRS administrative functions.

The State Revenue Service has established efficient collaboration through tax conventions with tax administrations of the following EU states: Sweden, Finland, Denmark, the Netherlands, Ireland, the UK and Germany. As of 1 January 1999, exchange of information is possible with 18 states. Conventions with France and Italy were ratified by Latvia in 1997 (these should be ratified by the counterparts in the near future). Negotiations on conclusion of tax conventions are continuing with Belgium, Austria and Portugal, as well as with several non-EU states.

Statistics

The law “*On State Statistics*” from November 1997 fully complies with the Council Regulation on Community Statistics and has allowed the following progress towards compatibility with EU standards to take place:

- evaluation of the adoption of EU legislation in the sphere of statistics has been completed, thus determining concrete spheres in which more detailed research is necessary to prepare proposals for amendments in order to implement the *Acquis*;
- the *Eurostat* Classification of Types of Constructions CC was introduced last year; the PRODCOM List 1998 (the *Eurostat* Classification of the Industrial Production) was

introduced to ensure EU-compatible information on state economic and social development. The implementation of the Statistical classification of products by activity (CPA) is planned for the beginning of the year 2000;

- the concept of the Integrated Statistical Data Processing and Management System and its tender specification has been completed;
- A law “*On the Population Census*” , which is in accordance with EU requirements, will be adopted by the Saeima before the end of this year. In 1998 the data processing of the first pilot Population Census was completed and the second pilot census test was taken in the first quarter of 1999. On the basis of these steps the instrumentality of the Population Census 2000 being developed. The pilot Agricultural Census took place in two regions and the obtained data will be processed completely before September 1999.
- The rural farms register is being developed, and its establishment procedure will be completed by the year 2000.
- The Central Statistical Bureau is continuing to improve its co-operation with other institutions. In 1999, co-operation between the Central Statistical Bureau and the Department of Citizenship and Migration Affairs in the construction of a Farm Register was improved. The Central Statistical Bureau has become more active in the working group on foreign trade, as well as in determining indicators to be included in the Real Estate Register of the Cadaster Centre.

Upgrading of the statistical system is scheduled to be completed for 2003. Improvement of the statistical system is included as a priority in the National Programme for Adoption of the Acquis.

3.4 Sectoral Policies

Industry

The principal aim of the authorities is to implement business and industrial policies to achieve a coherent framework, with different sector strategies harmonised within the set of agreed priorities. The achievement of this priority is closely connected with other issues, important for revival and further sustainable development of national industry - elaboration of the National Development Plan, ISPA and SAPARD realisation strategies.

A firm basis for sound industrial policy was set in the *European Commission – Latvia Joint Assessment of Economic Policy Priorities of Latvia*, adopted in 1999. This paper clearly defines restructuring policies, needed to accelerate industrial output growth - privatisation, creation of a transparent and friendly business environment, attraction of foreign direct investment, assistance to SME's, export promotion, financial sector reform and balancing of regional development. The education and labour market policies are playing an increasingly important role in the implementation of industrial policy.

A horizontal industrial competitiveness policy has been gradually developed in Latvia through various governmental programmes: Medium Term Economic Strategy, National Programme of Quality Assurance, National Programme for the Development of SMEs, National Programme on the Regional Development of Latvia and National Programme for the Integration into the EU. Currently the National Programme on Foreign Trade is being drafted and could be presented to the Government by the end of first half of 1999, whilst the Industrial Strategy could be presented to the Government by the end of 1999.

Industry is a very important sector of the Latvian economy. In 1998 20.2% of Latvia's GDP was generated by industry. Industrial output reported strong growth in 1997 of 3.4%. The trend continued in the first half of 1998, until industrial growth slowed after the Russian economic crisis. Despite the demand shocks and loss of a considerable share of the CIS market, the industrial sub-sectors oriented to the EU and OECD export markets continued booming in 1998 and the beginning of 1999.

The privatisation and restructuring policies were the main mechanisms to revive the industrial sector. The vast majority of industry is in private hands. 90% of the gross value added contributed by manufacturing was generated by the private sector. Successful privatisation of the industry attracted the investments necessary for restructuring and raising competitiveness. In 1998 the manufacturing sector attracted 113.3 million LVL of foreign direct investment (17.5% of total FDI stock). The food processing industry, which generates 34% of value added in manufacturing, received the majority of FDI.

Liberal trade (presently 70% of the total trade turnover takes place under a free trade regime) is a very important precondition for rapid and successful restructuring of the industrial sector. In 1997, 48.3% of the manufacturing output was exported. Export of goods in 1998 compared to the respective period in the previous year in current prices went up by 10%. Exports to the EU increased by 27.3%, reaching 56.6% of total exports (48.9% in 1997). The main export groups in total exports were high value added goods - wood products (34%), products of metal industry, engineering (18.2%), and light industry products (16.7%).

In 1998, two major industrial sub-sectors showed positive growth. Compared to the previous year, output of food products grew by 1.1%, whereas production of wood products grew by 13.7%.

Agriculture

The main aim of agricultural policy is to convert agriculture into a sector that is able to integrate into the common European market. *Sectoral Development Policies* were adopted in December 1998 and the *Annual Agricultural Development Programme* was adopted in 1998.

In 1998, due to unfavourable weather conditions and the impact of the Russian crisis, agricultural production decreased by 4.8% when compared to 1997. The share of primary agricultural and hunting production in current prices was 4.6% of GDP in 1997 and 3.6% in 1998. The share of the food processing industry of GDP in 1997 was 8.4%.

Consequently, producers and government institutions are looking for new export markets of agricultural production in West European countries.

The negative trade balance has decreased with Germany, Austria, Sweden and Denmark in comparison with 1997.

By 1 November 1998, 96.4% of all land was registered in the State Land Cadastre. 86.8% of agricultural land is in private hands, of which 45% is registered in the Land Book. The number of registered units in Land Book indicates the volume of the commercial land market. Large-scale private farms use 47% of agricultural land. The average size of family farms has increased and is now 24 hectares.

A law "*On Plant Protection*" was adopted in the Saeima in December 1998, and the State Plant Protection Station has submitted draft regulations to the Government.

For the promotion of the external trade of food products, the EU veterinary and phytosanitary mission inspectors have evaluated the state veterinary supervision and control system of the State Veterinary Service. The State Veterinary Service examines and evaluates milk, meat and fish processing in accordance with EU requirements. As of 1 January 1999, 9 milk processing enterprises, 8 fish processing enterprises and 3 refrigerator ships are on the list of enterprises that have the right to export their produce to EU member states. 14 veterinary laboratories have received accreditation and comply with EU norms.

A concept of a data exchange network among the Sanitary Border Inspection Service and State Plant Protection Station has been prepared. A cattle identification and registration system already works successfully. The first stage of training of sanitary border inspectors has finished.

Forestry

To ensure sustainable development of this sector in connection with market oriented production and states international liabilities; a New Forest Policy has been adopted. Timber production and environmental goals are well balanced in this basic document. Implementation of Forest Policy is the first priority in the current activities of governmental forestry institutions.

The share of forest products in value of total exports has increased from 35% in 1997 to 39 % in 1998.

A methodology for inventarisation of key forest habitats was developed successfully and is currently being put into practice..

State grants for foresting abandoned farmland were allocated for the first time. To facilitate investments in forest regeneration, amendments to the law "*On Property Tax*" were adopted.

Fisheries

To ensure development of the fisheries sector and structural policy, the programmes "*Baltic Sea and Coastal Fleet Development Programme*" and "*Fish Industry Development Programme*" were created within the framework of the National Fisheries development programme. These programmes include measures for compliance of production facilities of the fishing fleet, fish processing enterprises and cold stores to EU hygiene requirements, as well as estimation of the financial means for the implementation of the above mentioned aims. The fisheries sector is included as a part of the draft of the Rural Development Plan.

The share of fisheries in GDP gradually decreased (0.2 % in 1997, 0.2% in 1998). The specific weighting of exported fish production in total export volumes of Latvia in 1998 was 3,1 %. The foreign trade balance of fish production was positive in 1998 (export- 33.1 mill. LVL, import: 16.0 mill. LVL, foreign trade balance: 17.1 mill. LVL).

In 1998, fisheries administration paid additional attention to harmonisation with EC regulations. These matters covered the creation of a fishing vessel register, a landing control and landing reporting system, a fish buyer registration and fish first sales notes system, introduction of principles of a common fish market system, i.e. fish size, freshness categories etc.

The Latvian Vessel Register of the Maritime Administration has improved the fishing vessel computerised data sheets in accordance with EC regulations. The National Board of Fisheries has already listed all fishing vessels permitted to fish beyond coastal waters. Individual fishers registration (including data on used boats and cutters) in coastal and inland waters started in January 1999. Further actions of implementation of the fishing vessel register in Latvia relates

closely to the start of PHARE technical assistance project on creation of fishing vessel registration in the Associated Countries.

There are technical and financial difficulties in practical implementation. They concern the control system for fishing (including satellite tracking), fish processing and fish trade, as well as restructuring of the fishing fleet, fish processing enterprises and cold stores in compliance with EU hygiene and sanitary requirements to ensure competitiveness in the EU market.

Energy

The topical issues in development of the energy sector at present are energy legislation approximation, privatisation and restructuring of energy enterprises and promotion of energy efficiency. For legislation, priorities are oil stocks and security of energy supply, and energy efficiency. Investigations in respect of establishment of internal energy market principles are also proceeding.

The law "*On the Energy Sector*", passed by the Saeima in September 1998, incorporates the main provisions of the EU energy directives:

- Security of supply and establishment of oil stocks will minimise risks of oil product supply difficulties. The EU directive-compliant reserve creation principles are being developed and gradual accumulation of reserves (within 5-10 years) will be maintained. The establishment and utilisation of reserves are stipulated in the law "*On the Energy Sector*" and will be specified in regulations of the Government;
- Transparency of electricity and gas prices - necessary measures are already being taken by the Energy Regulation Council;
- Energy efficiency;
- Internal energy market;
- Transit of electricity and gas via networks.

At present, elaboration of drafts of subsidiary normative acts to implement the law "*On the Energy Sector*" is taking place.

To ensure creation of oil stocks, several draft regulations and amendments to existing legislation have been prepared by the Ministry of Economy. In order to regulate the supply of energy in case of an energy crisis, amendments in "*Regulations on Supply and Use of Electrical Energy*", "*Regulations on Supply and Use of Gas*" and "*Regulations on Supply and Use of Heat*" were adopted by the Government in March 1999.

The Regulations "*Order of Establishment and Storage of Reserves of Oil Products*" will be adopted by February 2000.

In October 1998, the Saeima ratified the Energy Charter Protocol on Energy Efficiency and Related Environmental Aspects.

Funds for implementation of energy efficiency projects are provided within the framework of the Annual State Investment Programme.

The process of liberalisation of the energy sector took place through the adoption and implementation of the law "*On the Energy Sector*" (September 1998) and secondary regulations of the Government. Until the end of 1998, the Latvian Energy Regulation Council issued 30 licences to electricity supply utilities, 73 – to heat supply companies, 4 – to natural gas companies, 7 – to Liquid Natural Gas supply companies. With the development of Combined

Heat and Power facilities in 1999 it is expected that approximately 10 companies will submit applications for licences.

Electricity, natural gas and heating tariffs in 1998 were determined according to the cost recovery method, combined (for natural gas) with the price cap method with generation, transmission, distribution and sale cost treated separately. When tariffs are approved it is assumed that user payments should cover:

- actual cost of energy generation, transmission, distribution and sales;
- profit to pay taxes, interest rates and dividends;
- capital contributions for the development of the company approved by the Energy Regulation Council.

Within the framework of the state programme, several regulations on hydrocarbons have been prepared. In order to establish an appropriate legislative environment for oil exploration, amendments to the law "*On continental shelf and economical area of the Republic of Latvia*" and in the law "*On taxes and fees*" were adopted in October 1998. Amendments to the law "*On Natural Deposits*" were adopted in February 1999

The draft law "*On Regulation of Public Utilities*" with the concept of a future "superregulator" covering energy, telecom and other utilities (excluding water and heat) is in process. In April 1999, the Government approved the "*Concept of the Regulation of Public Services*". This Concept establishes independent regulatory authorities for all kinds of main public services, with the gradual merging of concerned authorities into one joint National Regulatory Authority.

Electricity consumption in the country has remained at the level of the previous year. In 1998 electrical power produced in Latvia satisfied 91.5% of the overall demand and only 8.5% was imported from Russia, Estonia and Belarus.

Transport

The favourable geographical position of Latvia encourages transit transportation. The share of value added produced by the transport and communications sector in 1998 was 14.2%. In November the law "*On Railways*" came into the force, streamlining the legislative basis of this sector.

The Ministry of Transport consistently works on harmonisation of national road transport legislation with that of EU, regarding this process as one of the key issues for access to the EU road transport market. The regulation on licensing of entrepreneurial activity in order to engage in commercial carriage by road, in force as from 1 January 1999, is in full compliance with Directive 96/26.

The Regulations of the Government's "*Road traffic Rules*" are in compliance with Directive 96/53. The Regulations of the Government on Usage of Recording Equipment have been passed, providing compliance with the Council Regulation 3821/85 and AETR requirements. Regulations governing carriage of dangerous goods by road are being drafted.

Consistent work on providing a legal basis for introduction of the type approval system is continuing. *Regulation on Conformity Assessment of Wheeled Vehicles and their Components* was adopted by the Government in March 1999. It is based on Type Approval framework Directive 70/156 as amended by Directive 98/14 and establishes a legal base for this system in

Latvia. The next step will be adoption of a regulation which will transpose approximately 160 type approval directives.

To improve road safety under the framework of the Government Declaration, a National Programme for Road Traffic Safety is being planned.

Since November 1998, when the law “*On Railway*” came into the force, several secondary legal acts have been accepted by the Government, dealing with Procedure for opening, closing and naming of railway stations; Procedure for state registering and accounting of railway infrastructure; Procedure and criteria for issuing safety certificates to railway operators, suspension and annulment of operation; Statute of the Railway Infrastructure Fund; Regulations on railway safety belts, and Regulation of licensing railway operators; Statute of Railway Administration; Statute of Railway Technical Inspectorate; Procedure for entering into contracts for state orders for railway carriages ; Regulations on medical contraindications that prevent a person from qualifying as a railway specialist and performing these duties; Railway technical operators regulations.

The Railway Administration has been established and will become operational in 1999. The Railway Technical Inspectorate has been established as an independent public institution according to the law “*On Railways*” and will become operational in 1999. The provisions that regulate the functions of the institutions have been set. The main functions of the Railway Administration are: to ensure fair opportunities for rail use in allocating and charging for track access between different operators; to promote competition and prevent the abuse of any dominant market position; and to protect the interest of railway passengers. The Railway Technical Inspectorate controls safety issues according to legal acts.

In January 1999 the Railway Standardisation Technical Commission was established. The Commission will work out programmes of standardisation.

Qualitative and effective public transport is a priority. A law “*On Passenger Carriage*” is being drafted in order to implement state policy for passenger transport.

The priority of the Government in air transport is to conclude a Common European Aviation Area agreement. The Latvian Air Transport policy paper reflecting compliance of the general principles with the EU Air policy was accepted by the Government on 25 May 1999. It emphasises the main target – to develop an effective air transport system for optimal integration into the European and global air transport system. The harmonisation of technical requirements and administrative procedures in the field of civil aviation (Joint Aviation Regulations), set out by Joint Aviation Authorities, will be finished by the end of 1999.

The main priorities of the Government in the maritime sector are safety of navigation, including protection of marine environment, and facilitation of development of the Latvian shipping industry by framing and implementing a clear State maritime transport policy (adopted in July 1998 by the Government).

To increase maritime safety, as required by relevant IMO instruments, a building for a vessels traffic system, the VTS Tower in Riga was built in 1998. In May 1999, VTS equipment was installed and the vessel traffic system began operating. The modernisation of VTS in Ventspils and Liepaja port has been completed. The remaining VTS projects will be accomplished in accordance with the approved timetable until 2002.

In February 1999 the Government ratified the Salvage Convention. From December 1998 until April 1999 Latvia was conducting bilateral negotiations with Estonia, Sweden and Lithuania on maritime and aeronautical search and rescue in order to implement the requirements of SAR

Convention 1979 regarding the establishment of regions of responsibility and co-operation between the neighbouring countries. It is expected that by the end of this year SAR agreements with all three neighbouring states will enter into force.

Protocol 1988 of the SOLAS Convention, which is a last precondition for adopting national legislation on port state control, was adopted by the Saeima in March 1999. In May 1999 the Ministry of Transport adopted regulations "*On Port State Control*" implementing the relevant provisions of EC directives. The regulations regarding information on dangerous goods and ships registration transposing respective EC measures will be adopted by the Ministry of Transport in 1999. Draft legal acts have been submitted to interested ministries in order to restructure Maritime Administration of Latvia to be an effective and competent maritime authority.

The New shipping policy will be launched by the end of this year. This will provide a favourable environment for shipping companies to improve their competitiveness when operating from Latvia.

Small and Medium Enterprises

Currently SMEs account for 99% of all enterprises registered in Latvia. About 60% of the economically active population of Latvia is employed in SMEs. The SMEs are dominant in the major export industries, such as wood processing, foodstuffs and textiles.

Overall, Latvian SMEs policy from the legal point of view is fully aligned with EU requirements in this sector. A network of nine Business Advisory Service Centres (BASC) has been established. In addition, four Business Innovation Centres (BIC) have been established to support technology-oriented SMEs and promote the transfer of new technologies. The network of BASCs and BICs has been extended with assistance from the PHARE SME support programme. Nevertheless, the main concerns in this sector are associated with the financial resources available for the development and extension of the SMEs development programmes.

The Latvian Guarantee Agency was established in January 1998 as a non-profit limited liability company. The Latvian Guarantee Agency reserve capital is 0.95 million LVL. The aim of the Latvian Guarantee Agency is to promote investment financing for SMEs by sharing the risk with commercial banks. According to the Agreement between the Latvian Guarantee Agency and the Bank of Latvia, the Bank has acknowledged that the warranties, securities and guarantees issued by the LGA to credit institutions of Latvia shall be considered as equal to guarantees of the Government. Investment projects shall be promoted on the condition that they contribute to the competitiveness of the Latvian SMEs and that they show positive effects on the development of the commercial sector in Latvia. The guaranteed percentage under the funding guarantee is up to 70% of the creditor's claim and may be adjusted according to the financing requirements of the investment project.

3.5 Economic and Social Cohesion

Employment and Social Affairs

The changes in the registered unemployment rate show that until the Russian crisis the unemployment rate was going down. However, from June 1998 it started to rise, especially in October. According to the data of the State Employment Service, at the beginning of October 1998 the unemployed constituted 7.6% of the economically active population. The number of registered unemployed persons increased to 10.1% at the beginning of June 1999.

The main direction of labour market policy is to promote professional training and retraining of the unemployed. The Government in its Declaration on Proposed Activities plans to *inter alia* address issues of employment based on professional orientation at school, adapting of vocational training system to the needs of the labour market. Special labour market programmes have been developed for the unemployed with fewer possibilities to compete, the long term unemployed and the disabled. In 1998, of all unemployed people who received professional training, 37.8% were soon employed. Allocated funds for professional training and retraining from the state budget increased by 68 % in 1998 compared to 1997. In 1998 there were two PHARE projects for Employment service staff to support policy development in the pre-accession context/

In April 1999 the Government approved the concept *On Employment Promotion in the State* which prescribes: (1) elaboration of a National Action Plan for Employment; (2) creation of an Employment Council within the framework of the National Tripartite Consultative Council in order to improve the collaboration of state institutions, employers and trade unions in resolving of employment issues; (3) improvement of the financing mechanism for employment. Financing of the National Action Plan will be carried out within the limits of budget of the Ministries responsible for the respective item, and employment issues will be given higher priority in the State Investment programme and National Indicative Programme.

The draft law "*On Labour Protection*" transposes EU requirements of the framework Directive in the field of health and safety at work on the introduction of measures to encourage improvements in the safety and health of workers at work. It is expected that the draft law "*On Labour Protection*" will be adopted at the end of 1999.

New legislation has been adopted in the field of health and safety in the workplace regarding the protection of workers from risks related to exposure to asbestos, on the provision of safety and health signs at work, and on the investigation and registration of the accidents in the work place.

The following draft regulations of the Government are under preparation (expected to be approved until the end of 1999): "*On the Minimum Safety and Health Requirements at the Workplaces*"; "*On the Minimum Requirements of Safety and Health Protection of Workers Using Work Equipment*"; "*On Labour Protection in Work With Display Screen Equipment*"; "*General Requirements on Labour Protection in Building and Construction*"; "*On the Minimum Safety and Health Requirements for the Manual Handling of Loads Where there is a Risk Particularly of Back Injury To Workers*"; "*On the Protection of Workers from the Risks Related to Exposure to Chemical Agents at Work*". These regulations implement the requirements of EU.

The Government in March 1999 adopted the draft law "On the Protection of Employees in the Event of Insolvency of Their Employers". The adoption of the law by the Saeima is expected by the end of 1999.

A new draft "*Labour Code*" has been prepared in conformity with requirements of the *acquis* on collective redundancies, on implementation of the principle of equal treatment for men and women in employment, vocational training, promotion and working conditions, on equal pay, on the safeguarding of employees' rights in the event of transfer of undertakings, business or parts of business, on the protection of young people at work and organisation of working time, on part-time work, burden of proof, parental leave. The preparation of the draft is at the final stage of consultations with social partners. It is expected that the draft Labour Code will be submitted to the Government in August and to the Saeima in September 1999. The Labour Code is expected to be adopted by the Saeima in April 2000.

At the beginning of 1999 the State Labour Inspection (SLI) had 180 staff members and 7 regional offices. Strengthening of the SLI and approximation of legislation has been facilitated by the PHARE programme and by assistance from the Swedish Government.

For improvement of social dialogue on employment issues, the Latvian Tripartite Consultative Council of Employers, Government and Trade Union representatives has been reformed as the National Tripartite Co-operation Council in October 1998. The first session of the Council took place in March 1998, when legal acts in the social sphere and an activity programme for 1999 were considered.

In the nearest future internal rules and regulations of the National Tripartite Co-operation Council, as well as the division of its sub-competencies and model-regulation of the sub-councils, will be elaborated and approved.

In August 1999 the draft “*Mechanism of Labour Dispute Settlement*” will be submitted to the Government and during 1999 the draft law “*On Labour Dispute Settlements*” will be elaborated.

In order to strengthen the co-operation in the field of social dialogue, the law “*On Employer's Organisations*” was adopted by the Saeima on 29 April 1999.

The health care system has been improved on the basis of four key points: institutional changes, improvement of financial flow, increasing the quality of health care services and establishing the concept of family medicine.

To continue improvements to the health care system in Latvia and achieve effective utilisation of resources assigned for this purpose, in co-operation with the World Bank, the Ministry of Welfare has commenced a long-term development programme to support Latvian Health Reform. The goal of the Latvian Health Reform Programme is to improve the effectiveness, quality and availability of health care services to the population.

The Ministry of Welfare is responsible for implementation of three directives, 93/42/EEC, 90/385/EEC and 84/539/EEC. These three directives are to be implemented completely by the end of this year.

Regional Policy and Cohesion

Latvia's regional development policy focuses on the reduction and elimination of regional social and economic imbalances.

An important factor for the development of regions is territorial reform. It is aimed at setting an agenda to establish economically sustainable local authorities. The law “*On Administrative Territorial Reform*” was adopted by the Saeima in October 1998. A policy for creation of regional structures is being created by a government task force. It is expected that in the nearest future ‘The Concept of Regional Administrative Territorial Division’ will be submitted to the Cabinet of Ministers for adoption.

The National Regional Development Programme (NRDP) is under elaboration. It will provide a framework for the institutional, policy and implementation structures for regional development. The NRDP will promote the necessary move from a highly centralised sectoral policy development and implementation system to a more decentralised integrated regional approach.

Considerable progress in structural policy development has been made. The National Development Plan (NDP) is being prepared in line with the National Programme for the Adoption of the Acquis and envisages key policy priorities for structural adjustment of the economy. The

National Aid Coordinator (Minister for Special Assignment for Cooperation with International Financial Agencies) is politically responsible for the supervision of the elaboration of the NDP. The representative (Deputy State Secretary) of Ministry of Finance presently is leading the horizontal working group for preparation of the Plan. The Ministry of Environmental Protection and Regional Development, other key line ministries and the European Integration Bureau (responsible for the NPAA) are all contributing to the preparation of the NDP. The NDP will combine programmes funded by the national budget, including loans, pre-structural funds (ISPA and SAPARD) and PHARE.

The Government implemented its policy objectives by establishing the Regional Fund and by creating a rural development programme supported by a World Bank loan (14.75 million LVL). The Regional Fund promotes entrepreneurial activities in selected regions. The Regional Fund will in the future not only support SMEs but turn towards more integrated support programmes.

The Regional Development Council (RDC), established in 1998, is the institution in charge of co-ordination of regional policy activities and bears the responsibility for regional policy development. The RDC consists of representatives from both Government and Parliament. The RDC monitors the Regional Fund towards co-ordination of regional policy documents such as the National Regional Development Programme.

The ministries involved in policy implementation by drafting laws and programmes for sector development are the following: The Ministry of Environmental Protection and Regional Development is primarily responsible for regional policies, dealing with regional development planning and spatial planning; the Ministry of Economy is responsible for regional economic policy through the Regional Fund and is responsible for SME development and export and FDI promotion; the Ministry of Agriculture is responsible for development in rural areas, including economic diversification; the Ministry of Transport focuses on the rural and regional road investment programme. The Ministry of Welfare is participating in the preparation of social assistance policy and health care policy and in the co-ordination of employment issues at the regional level. The Ministry of Education and Science is responsible for Human Resources Development (HRD) and has set-up a regional pilot project in order to decentralise HRD.

To improve the co-ordination of different activities in the preparatory process for the Structural Funds, an Inter-ministerial Structural Funds Working Group has been in operation since March 1998. The Structural Funds Co-ordination Division (SFCD) within the Foreign Assistance Programmes Co-ordination Directorate has, at a working level, the leading role in the preparation process for Structural Funds under the supervision of the National Aid Co-ordinator (by a Decision of the Cabinet of Ministers of April 1999). The SFCD takes the role of the Central Co-ordination Unit (CCU) for the Special Preparatory Programme for the Structural Funds in Latvia (SPP).

The establishment of a regional level of between 5 and 9 regions is in progress and will be the basis for institutional capacity building at the regional level (close to NUTS III level regions) according to *“The Law of Territorial Development Planning”* and *“The Law of Administrative and Territorial Reform”*.

The establishment of a regional development agency in each region was started at the beginning of 1999. The first agency to be established is the Latgale Regional Development Agency. The RDAs will become the focal points for the decentralised regional policy programming, implementation and monitoring.

As a precursor for the RDAs, the Latvian Government established a special company/institution (Regional Development) to assist with the implementation of the projects supported by the Regional Fund. The Advisory Committee of the Regional Fund selected 118 projects in 1998.

The National Territorial Planning Centre (March 1999) is capable of technically and methodologically supporting development planning in the regions and to assist local governments in the elaboration of the National Spatial Plan.

The reform of the current 26 departments of the Ministry of Agriculture into 5 new regional agricultural departments (according to the overall regional structure) will constitute the administrative structure for agricultural programmes (including the management of SAPARD funds). Rural development and rural infrastructure projects will be channelled through Partnership Councils created at the regional agricultural departments.

All the practical arrangements for the implementation of the Special Preparatory Programme have been undertaken in order to begin in September 1999. In September 1998, 5 working groups were set-up for preparing the implementation of the SPP. Interministerial working groups each focuses on a particular area of the SPP: National Development Plan, Sound Financial Management, Legal Framework, and preparation for ISPA and SAPARD.

The main ministries involved in the preparation for ISPA are the Ministries of Transport and Environmental Protection who are responsible for developing the projects. The Ministry of Finance, the Ministry of Economy and the Directorate for Foreign Assistance Programmes Co-ordination are responsible for co-ordination with other resources, the budget and the public investment programme.

The Ministry of Agriculture established the Agency for Rural Structural Programmes at the end of 1998. The Agency will be the main implementing institution of SAPARD from 2000. The Rural Development Division (under the Department of Agricultural Strategy and Co-operation in Ministry of Agriculture) was established in December 1998 to supervise the formulation, control and strategic guidance of the rural development policy and to co-ordinate the SAPARD rural development plan.

3.6 Quality of Life and Environment

Environment

Overall development complies with the objectives and short and medium term priorities of the Accession Partnership.

With the assistance of PHARE DISAE Facility projects, implementation programmes for all environmental sectors are developed.

It is envisaged that the EU environmental *acquis* will be transposed into Latvian legislation by the end of 2002.

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

Air. Considerable progress was made in transposition of the Air Framework Directive and its daughter directives, as well as Directives on Large Combustion Plants and Fuel Quality.

The Government adopted a regulation "*On the Environmental Norms for Fuel Quality*" in July 1998. This Regulation brought Latvian legislation into harmony with fuel quality directives.

Regulations “*On Air Quality*” were adopted in June 1999. Regulations “*On the Elimination of Air Emissions from Stationary Air Pollution Sources*” were drafted and are expected to be adopted by the Government by October 1999. Regulations “*On the Environmental Requirements for Petrol Stations, Terminals and Mobile Containers*” are being drafted. With adoption of these legal acts almost all EU legislation on air protection will be transposed.

Waste. In October 1998 a new law “*On Municipal Waste*” was adopted, bringing Latvian legislation into harmony with most of the provisions of the Waste Framework Directive.

In February 1999 two regulations of the Government were adopted: “*On Municipal Waste Classification*” and “*On Siting, Management and Closure of Landfills for Municipal Waste*”.

A series of legal acts are in the drafting stages, pursuant to the law “*On Municipal Waste*”: regulations “*On Permitting Procedure for Municipal Waste Recycling and Disposal*”, “*On Register of those Legal and Physical Persons who Provide Municipal Waste Collecting, Storage, Treatment, Transfer and Transportation Services*”, “*On Order for Estimation of Municipal Waste Management Fees*”, which will be adopted in 1999.

In order to fulfil all requirements of the Hazardous Waste Directive, amendments to laws and regulations are being prepared. It is planned that amendments to the law “*On Hazardous Waste*” will be adopted in the nearest future, amendments to the law “*On Municipal Waste*”, amendments to the regulations “*On the Order of Preparing Documents for Activities with Hazardous Waste*” and “*On Classification of Hazardous Waste and Hazard Criteria*” are expected to be adopted by October 1999.

The implementation of the programme on hazardous waste is successfully continuing. In 1998 and in the beginning of 1999 the collection of unwanted pesticides was accomplished. They are disposed of in a specially established storage facility. A decision about incineration of the collected pesticides has been made and will be carried out in a semi-mobile incinerator situated in Latvia.

Under the framework of the programme “*Municipal Solid Waste Management System in Latvia*”, further development of a regional approach to solid waste management has been elaborated in seven regions of Latvia. Implementation of the Northern Vidzeme solid waste management pilot project is continuing. A company for waste management has been established in the region. Environmental impact assessment was carried out for 3 potential landfill sites and sanitation of 8 existing dumping sites was carried out in the region.

Water. Latvia’s approach to the Water Framework directive is being developed. In August 1998 regulations “*On Requirements for Arranging and Hygiene of Places for Swimming*” were adopted, implementing the Bathing Water Directive. In February 1999 the Government adopted regulations “*On Obligatory Requirements for Harmless Drinking Water*”.

In November 1998 amendments to the regulations “*On Water Use Permits*” were adopted.

During 1998 wastewater treatment plants were completed in 5 cities; 17 investment projects prepared or continued; 6 feasibility studies finalised; 31 new feasibility studies started or tendered. Substantive efforts were devoted to enhance the skills and institutional capabilities of local authorities.

Industrial pollution. The Regulations fully transposing the EU Seveso directive – “*On the Control of Risk and Risk Management of Major Chemical Accidents*” have been prepared and are expected to be adopted by the Government by the end of the year. The Seveso licences will be issued from the beginning of the year 2000. The draft law “*On Pollution control*” transposing the

Industrial Pollution Prevention Control (IPPC) directive is under preparation and will be prepared by the end of the year. Together with the regulations and administrative framework which is under preparation, the implementation of the IPPC directive could commence from the beginning of 2001.

Nuclear Safety. The concept on the Radiation Safety Agency was elaborated and foresees the merger of the nuclear safety supervision services of the Ministry of Environmental Protection and Regional Development and the Ministry of Welfare.

The Concept of Decommissioning of the Nuclear Research Reactor in *Salaspils* and three alternative implementation projects of this Concept were elaborated.

Consumer Protection

A new “*Consumer Rights Protection*” law was passed by the Saeima in March and came in force in April 1999. The law implements disposition of several EC directives, including 93/13 on unfair terms in consumer contracts.

According to this law, Regulations “*On the Indication of Prices for Products and Services*” were accepted in May 1999 and will be in force from January 2000; the regulations “*On Consumer Credit*”, “*On Contracts Negotiated Away from Business premises*”, “*On Distance Contracts*” and “*On Contract on a Right to Use Building or Part of a Building Provided for Accommodation on a Timeshare Basis*” will be adopted by the Government in 1999. The regulations will transpose the corresponding EC directives.

The following regulations, harmonised with the *acquis*, are already in force: “*On the Safety of Cleaning Agents and Detergents*”; “*On the Safety of Cosmetics*”; “*On the Labelling of Textiles*”; “*On the Labelling of Foodstuffs*”.

Minor improvements are foreseen to the regulations “*On the Safety of Cosmetics*” and “*On the Labelling of Foodstuffs*”.

It is planned to adopt Regulations “*On Safety of Toys*”, “*On Labelling of Footwear*”, “*On Labelling of Crystal*” by the end of 1999.

The draft law “*On Advertising*”, which incorporates directives concerning misleading and comparative advertising has been submitted to the Government.

The Consumer Rights Protection Centre (34 employees), established in May 1998, is the main institution responsible for the supervision of observance of consumer rights protection legislation. The State Sanitary Inspection (180 employees), established in October 1997, is responsible for the protection of consumer rights in the area of circulation and distribution of foodstuffs, cosmetics and household chemicals.

The process of setting up regional consumer protection centres has begun.

The Consumer Interests Protection Association has been established. The Association unifies the regional NGO's of Consumer Interests Protection and enjoys the rights guaranteed by the “*Consumer Rights Protection*” law - to bring an action to court for the protection of consumer rights and interests and to represent consumer interests in court.

3.7 Justice and Home Affairs

In 1998 as well as in 1999, special attention has been paid to the reform of the judicial system in accordance with internationally recognised standards and to strengthening the fight against organised crime and corruption. International legal co-operation has also been promoted. The *Agreement between the Government of the Republic of Latvia and the Government of the Kingdom of Sweden on development of co-operation and technical assistance in the area of Justice and Home Affairs*, signed in December 1998, is being successfully implemented. Budgetary resources for the purpose of strengthening the Eastern border have been approved by the Government and daily renovations and enhancements are being made with the use of distributed funds.

Judicial co-operation

Judicial co-operation in criminal matters is developing on the basis of the Conventions of the Council of Europe. The three responsible institutions are the Ministry of Interior, the Prosecutor General's Office and the Ministry of Justice. The contact points within the Ministry of Justice and the Prosecutor General's Office to facilitate judicial co-operation, were communicated to the Council Secretariat in January 1999 with the goal to incorporate the Latvian authorities into the European Judicial Network. Preparatory works to implement the PHARE Horizontal project on the implementation of conventions in the penal area have begun. Considering the practice of the Prosecutor General's Office, the Ministry of Justice, and the Ministry of Interior, Latvia is ready to make a statement of good practice according to the Joint Action of 29 June 1998 on Good Practice in Mutual Legal Assistance in Criminal Matters.

Judicial co-operation in civil matters continues to develop. The *Lugano Convention of 16 September 1988 on Jurisdiction and Enforcement of Judgements in Civil and Commercial Matters* is being prepared for signing. The new Code of Civil Procedure contains the main provisions of the Lugano Convention on international jurisdiction and enforcement of foreign judgements. Other international conventions in the field of judicial co-operation in civil matters are also in the stage of preparation for accession. The Courts department of the Ministry of Justice makes the transmission of applications for enforcement. The actual co-operation is carried out in accordance with the bilateral agreements concluded by Latvia with third countries, and according to several multilateral conventions. In the first half of 1999, Latvia has received 193 requests, of which 77 have already been enforced. The Ministry of Justice has sent 119 requests of which 18 are recognised or enforced.

The fight against organised crime

The fight against organised crime is escalating gradually but surely. The disclosure rate on crimes, including organised crime and corruption has increased and in 1998 was more than 56%. In particular, the number of solved economic crimes increased, and the number of murders and crimes committed with handguns has fallen in the past year.

Latvia is actively participating in the Task Force on Combat of Organised Crime in the Baltic Sea region. The Bureau for Fighting Organised Crime and Corruption is currently working in co-operation with neighbouring states.

In accordance with the National Programme on Crime Prevention, the Anti-smuggling Co-ordination Centre was established in 1998 to improve co-ordination between domestic law enforcement agencies. The "*Criminal Law*", the amendments to the Code of Criminal Procedure and the law "*On Investigations*" guarantees effective protection of witnesses and victims.

On 4 March 1999, Latvia ratified *The European Convention on the Suppression of Terrorism*.

The State Police has specialised units to tackle specific crimes including divisions to deal with economic crimes, counterfeiting, securities and credit cards, and violations of intellectual property rights. A unit responsible for witness security was established within the State Police. A project - *USA (FBI) and ASF Stolen Vehicles* – is aimed at improving the mechanism for detecting criminals through use of computer database information. The State Police now can share information with the National Border Guard on vehicles crossing the border and their drivers.

Within the National Drug Enforcement Bureau, the National Contact Group with Europol's Drug Enforcement unit will be established in 2000. To cover all areas of activities, the number of staff members of the Drug Enforcement Bureau has been increased. Latvia's drug control and drug abuse prevention masterplan for the period 1999-2003 is being implemented. It has been provided with the necessary financing.

Border Control

Substantial state funding has been allocated for the strengthening of Latvia's Eastern Border. In 1999, 8,243 million LVL are allocated for this purpose (since 1992, a total of 5,75 million LVL has already been devoted to this task). A new international border-control point and two complexes for Border Guard sections were built in 1998 on the Eastern border. A border control and information system is also being set in place.

Since December 1997, the Latvia-Russia Border Agreement has been ready for signing. The maps are agreed and initialled and Latvia is taking the responsibility to prepare the border on its side. During the trilateral meeting of Latvia, Belarus and Russia in December 1998, a draft agreement was reached on determining and marking the border intersection point of the three states. The demarcation of the Latvian-Belarus land border is proceeding.

In 1999, the telecommunications network linking Eastern border posts with other agencies of the State Police is being upgraded. In 1999, infrastructure improvements on the Latvia - Belarus border include one international border control point (*Paternieki*), one complex for the Border Guard section and two surveillance towers. The purchase of cross-country vehicles, snowmobiles and patrol boats has been budgeted.

Under the leadership of the Ministry of Interior, a committee has been established to work out a draft concept for the Coast Guard.

Successful training of border guards is taking place at the Rezekne Border Guard School (one year programme) and at the Border Guard College established in the Police Academy of Latvia (a 2 year programme).

Asylum

The "Mucenieki" Reception Centre, as well as the "Riga Airport Short-term Reception Centre" were opened in 1998. From 45 applications for refugee status, 39 have been examined and on 1 June 1999 5 persons were recognised as refugees in accordance with the 1951 Geneva Convention relating to the Status of Refugees. 6 applications are currently under consideration. The Appeal Council in Refugee Matters is functioning properly.

The Citizenship and Migration Affairs Board is involved in the PHARE justice and home affairs horizontal programme on asylum issues in the framework of which a working group has been established in order to amend asylum legislation according to the EU acquis. Currently a draft

Concept of the Action Plan is being worked out and is expected to be adopted in July during a round table meeting.

3.8 External Policies

Trade and International Economic Relations

The average non-trade-weighted customs tariff rate for industrial goods has declined to 3,71% (basic rate) and to 2,47% (MFN rate), with customs tariffs having been reduced to zero or a 1% rate on many goods. In respect to agricultural products, the average non-trade-weighted tariff was reduced to 14.7% at the end of 1998.

Latvia's accession to the WTO was approved in October 1998. Latvia became a full-fledged member of the WTO on 10 February 1999. Latvia has aligned itself very closely to EC Common Commercial Policy, including the EC's GATS commitments. Latvia has made progress in aligning its commercial defence instruments with international standards. The law "*On Safeguards*" was adopted in February 1999, the drafts of the law "*On Anti-Dumping*" and the law "*On Countervailing Duties*" are under completion.

Latvia continues to align itself with the EC Common Commercial Policy by becoming a party to various preferential trade agreements. A Free Trade Agreement with Hungary was signed on 10 June 1999. Negotiations on Free Trade Agreements with Bulgaria and Romania are taking place.

Co-operation among the Baltic States in implementing gradual liberalisation and regional integration policies is developing and a Baltic Common Economic Area is being introduced. An agreement on the abolition of non-tariff barriers to trade was concluded in November 1997, and came into force in July 1998. Negotiations are proceeding on liberalisation of the services market.

Development

Latvia has no specific budget allocation for development aid, but has granted development aid on a case-by-case basis. No GSP schemes are being applied in Latvia.

Customs

The new "*Customs Law*" implements EU requirements, the Kyoto convention and the WTO Agreement, and is fully operational. Nevertheless, some spheres have been identified where additional implementing rules would be expedient to ensure completely uniform application of the norms. The provisions concerned will be adopted during 1999.

In October 1998 amendments to the "*Customs Law*" were adopted in respect to relief and temporary imports after recommendations expressed in the Association subcommittee meeting.

Following the remarks made in the European Commission's Progress Report on the problems in the field, two tasks were undertaken:

- In February 1999 the Government adopted the regulations "*On Customs Control Measures for Protection of Intellectual Property Rights*", which will come into force in July 1999.
- The Ministry of Finance submitted the draft regulations "*On Binding Tariff Information*" to the Government in February 1999.

As regards the international instruments on customs procedures, Latvia plans to ratify the International Convention relating to Temporary Admission (Istanbul Convention) by the end of

1999. Latvia is already a Contracting party to conventions such as the Customs Convention on the International Transport of Goods under the Cover of TIR carnets, International Convention on the Harmonised Commodity Description and Coding System, International Convention on Mutual Administrative Assistance for the Prevention, Investigation and Repression of Customs Offences (Nairobi Convention) and International Convention on the Simplification and Harmonisation of Customs Procedures (Kyoto Convention).

Joint transit control based on the principles of EU/EBTA Common Transit Agreement started between Latvia, Estonia and Lithuania in June 1999. This is a significant step towards accession to the Convention on a common transit procedure.

The installation of the ASYCUDA++ system, which has been selected for the computerisation of Customs revenue collection, is at the pilot stage (95% of the national system has been created). Initially, the system will be introduced at three pilot sites during 1999 and subsequently it will be implemented across all other customs offices in a national rollout programme scheduled for completion in 2001.

A revised flow path for dealing with passengers and freight is being introduced progressively at customs checkpoints to take account of the changes necessary to ensure successful implementation of ASYCUDA.

To ensure that the customs procedures are in compliance with the respective EU norms, systems for customs value and post-importation audit are being introduced. The necessary regulations have been prepared for effective introduction of a post-importation audit mechanism. A support system for guarantee mechanisms and a customs debt administration system is being introduced. Necessary structures are being created to meet EU requirements on customs control measures for the protection of intellectual property rights.

The Information Sub-division of the Customs Board Anti-Smuggling Division was created in January 1998. The following structures were created within each regional Anti-smuggling Division in July 1998: Intelligence Unit, Investigation Unit, Operational Work Unit and Mobile Unit. The computerised risk analysis system (TIMS) is being introduced in Latvian customs. The TIMS Border Alert system is installed in 8 customs checkpoints.

Infrastructure of customs checkpoints, especially on the Eastern border, is constantly being improved. Joint customs checkpoints are being established with Estonia and Lithuania - the initiative is supported by the EU.

Common Foreign and Security Policy

Latvia is involved in the multilateral political dialogue within the framework of the Common Foreign and Security Policy. It has aligned itself with or supported the EU Common Positions and Joint Actions within the EU CFSP. The national policy of Latvia has been in compliance with the respective EU activities.

Latvia supports further strengthening of the European Security and Defence Identity. This process is compatible with Latvia's efforts to prepare for NATO membership, including the strengthening of Latvia's defence capabilities. To this end, Latvia's NATO Integration Council was created and the NATO Integration Plan was approved in October 1998. Latvia's defence budget for 1999 was increased by 43%, including a major increase directed towards international co-operation activities.

As a WEU Associated Partner Latvia participates in the activities of WEU, which constitutes a part of the overall European integration process. In 1998 Latvia took an active part in the WEU

exercise CRISEX 98, and plans to take part in the next one- CRISEX/CMX 2000, carried out jointly with NATO.

Latvia is prepared to support the EU Joint Actions upon its accession to the European Union, and when necessary, take part in them. Six observers from Latvia were sent to participate in the OSCE Verification Mission in Kosovo in 1998. In April 1999 eight medical specialists for the NATO-led operation “Allied Harbour” were sent to provide military support to the international relief operation in Albania. In May 1999 Latvia provided humanitarian assistance for Kosovar refugees in Macedonia. Latvia joined the EU petroleum and petroleum products embargo against the Federal Republic of Yugoslavia.

Latvia has submitted to the European Commission a proposal for the EU Northern Dimension initiative and is prepared to take an active part in its implementation. Latvia contributes to regional stability through active co-operation in the Baltic Sea Region.

Conducting its foreign policy as a future EU member-state, Latvia has no difficulty in continuing to align with the CFSP acquis, and, with the relevant institutions and instruments in place, will be ready to fully assume all the responsibilities under the CFSP and co-operate actively within this framework upon accession to the EU.

3.9 Financial Questions

Latvia has taken further steps to ameliorate the functioning of the system of audit and financial control.

Legislation in the sphere of external audit almost completely complies with INTOSAI Lima declaration requirements. Being aware of its significant role in control of the use of EU funds from future Structural and Cohesion funds, the State Audit Office (SAO) (173 persons) has undertaken extensive preparatory work with a view to smooth and flexible adjustment to the respective EU requirements. A new department was established to facilitate effective audit planning, co-ordination, quality control and audit methodology. SAO plans to undertake audits of several projects involving EU funds in the year 1999.

To ensure full compliance with the law “*On the State Audit Office*” with EU requirements, the appropriate amendments are expected to be prepared by the end of 1999, defining the powers of SAO in accordance with INTOSAI Audit standards terminology and clarifying the scope of audit work.

The other important task is to ensure implementation of the new Audit Manual (“Coopers&Lybrand” has produced the first Audit Manual for SAO in the Baltic States. Procedures provided for by the manual are fully compliant with those of the EU. Implementation of the manual will allow a switch from relatively narrow legality audits to a full range of modern audit techniques covering financial and performance aspects. It is envisaged that the manual will be implemented by mid-2001.)

Internal Audit units have already been established in a number of government institutions. In February 1999 the Government mandated the Ministry of Finance to be co-ordinator of the implementation of an internal audit system in Latvia. The concept paper on the internal audit control was approved by the Government in March 1999. Drafting of the new Government regulations “*For internal control*” was finalised in mid-April. The regulations will not only contain standards for performance of internal audit in the Latvian public service, but also provide for the introduction of independent internal audit units in all ministries, the scope of internal audit work, auditing of Community funds, Internal Audit Council, Annual Controls Assurance

Statements and reporting of internal audit work. It is planned that major support for Internal Audit will be received from the PHARE Public Administration Reform Project. The first joint audit of PHARE projects was carried out by representatives from the Ministry of Finance and two key line ministries in May 1999 within the Public Administration Reform Project, under supervision of experienced EU internal audit experts.

For the management of Community assistance beginning from the financial year 1998, the Ministry of Finance has established the National Fund System. The National Fund will be responsible for payments on contract, analytical accounting and financial reporting. The Internal Audit Departments of the Ministries will undertake the control functions in question. A Joint Monitoring Committee will be established to monitor the progress of programmes.

4. Administrative Capacity to Apply the Acquis

4.1 Administrative structures

The Public Administration Reform agenda has the following key features:

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

In March 1998, the Cabinet adopted a medium-term public administration strategy and an Action Plan with a range of priority tasks including eliminating duplication of tasks between Ministries, pay reform, career development, internal audit, territorial reform, budget reform and transparency issues (such as the Ombudsman and anti-corruption strategy).

The Saeima and the Committee of European Affairs in Saeima provide the political continuity of the process. The Committee of European Affairs assesses the compatibility of new legislative acts with EU legislation.

The European Integration Council (EIC) is a high level political institution established by the Government for political administration of the European integration process. The EIC is composed of seven ministers representing the seven ministries most involved in the integration process.

The Council of Senior Officials (CSO) is an institution accountable for the horizontal practical co-ordination of the integration process. It is composed of the senior officials responsible for the European integration in all the ministries, and of the representatives of the State Bank, the Public Administration Reform Bureau, and the State Chancellery. The director of the European Integration Bureau heads the CSO. The CSO has formed more than 30 inter-ministerial working groups, which cover the acquis, as well as issues of the second and the third pillars.

The European Integration Bureau (EIB) is the central administrative institution for the co-ordination of the internal integration process of the state. It functions as a secretariat for the CSO and the EIC. The EIB is responsible for the harmonisation of national legislation, supervision of implementation of the national integration programme, preparation of conclusions about conformity with EU laws, and co-ordination of the work on information to the public.

The Ministry of Foreign Affairs is the central institution for the administration and organisation of the external integration process. The ministry supervises and administrates the external integration process of Latvia.

The Negotiation Task Force ensures preparation of Latvia's accession negotiations, and preparation of a draft accession negotiation mandate.

The Bureau of Public Administration Reform (BPAR) screens draft regulations and draft laws to ensure that proposals for changes to public functions, structures of public administration institutions, institutional status, and the status of civil servants or government employees are in line with the overall concept of public administration reform. In addition, the Bureau ensures that draft laws avoid conflicts of interest and situations of overlapping competencies both at institutional and management level. The responsibility of the Bureau for Public Administration Reform is in co-operation with ministries and in conformity with the National Programme of Adoption of *acquis* to prepare a National Institution Building Plan that lays out the goals, objectives and measures for raising administrative capacity to support democracy and enforce *acquis*.

The Bureau of Public Administration Reform reviewed the functions and structures of the Ministry of Agriculture in February 1999. The review of functions included a programme for the restructuring of the system of institutions in order to clarify the mandates of responsibilities of institutions and to adjust the level of staffing for the assigned functions and tasks.

To increase accountability of public institutions, in December 1998 the Government passed an Instruction "*On Public Annual Reports*" to be prepared and published by each public entity.

Development of human resource management policies in the civil service was made possible through the establishment of an interministerial Council of Personnel Managers, co-ordinated by the Civil Service Administration. Management Audit and personnel changes in the civil service facilitated the co-ordination of Civil Service Administration related to overall management of the civil service. Strengthening of the civil service through training and better implementation of "*Civil Service Law*" is supported by the on-going PHARE project on support to Public Administration Reform.

4.2 Administrative and judicial capacity: key areas for implementation of the *acquis*

Single market: Latvia has established the necessary institutional infrastructure in the field of free movement of goods. Substantial efforts continue to be made to strengthen the enforcement capacity in the field of intellectual and industrial property.

The State and Municipal Procurement Monitoring Department (6 persons) within the Ministry of Finance has during the past year developed its capacity to monitor the implementation of procurement law. It is foreseen that in a year's time the powers of the surveillance structure will be widened – its decisions will become binding for procuring entities.

The Latvian National Accreditation Office, LATAK, under the supervision of the Ministry of Economy, accredits testing laboratories, calibration laboratories, certification bodies and inspectors. A number of technical committees form branches of LATAK.

In January 1999, after the reorganisation of the Latvian National Standardisation and Metrology Centre, the Latvian Standard, Latvian National Metrology Centre, and State Metrology Inspection were established.

In March 1998 the Government established a Consumer Rights Protection Centre (34 persons) under the Ministry of Economy. Its competence is to control the observance of consumer rights in the areas of goods and services (excluding areas such as food, veterinary issues and pharmaceuticals, which are controlled by other institutions).

Concerning free movement of services, the banking sector has been strengthened owing to strict supervision by the Bank of Latvia. Efforts are also being undertaken on the supervision of the non-banking sector.

From September 1999 Riga Technical University is introducing an Actuary Masters course .

Customs and indirect taxation: the State Revenue Service employs 4504 officials, including 643 employees in the SRS Central administration and 3861 in SRS regional offices (34 full-fledged regional offices and 184 customs points).

The modernisation process of the SRS was streamlined in 1998, when a 5-year modernisation project was launched. This covers all strategically important areas of development, notably – establishment of a 3-level SRS structure, improvement of management techniques, improvement of the tax audit function, strengthening internal control, further computerisation. (see chapter 3.).

Agriculture: The Department for Control of Products of Animal Origin operates under the auspices of the State Veterinary Service. 120 food quality inspectors have been trained. There is a division of competence between the Ministry of Agriculture and Ministry of Welfare in the scope of state supervision and control of food circulation. Since 1999 the state control institutions are carrying out the regular inspections in accordance with surveillance programmes. A milk reference laboratory has been established.

Latvia is strengthening co-ordination of EU accession-related work within the Ministry for Agriculture, by the training of personnel in EU law and by allocating additional resources to the legal approximation process, in particular as regards veterinary, phytosanitary and food control areas.

Transport: The Railway Administration has been established and will become operational in July 1999, the Railway Technical Inspectorate has been established and will become operational in July 1999 as required in the law “*On Railways*”. The maritime and port administrations have increased their activities to improve maritime safety performance. The institutional structures in the field of aviation are well established.

Employment and social policy: The Ministry of Welfare is responsible for new pension reforms and social protection systems. The administration has recently been reinforced. The State Social Insurance Agency is responsible for administrating functions of the State in social insurance services. Branches administered include old age, invalidity, sickness, maternity, unemployment, occupational accidents and diseases, family benefits, death grants, social security benefit. The SSIA is currently involved in the implementation of bilateral social security agreements binding to Latvia.

Regional policy and cohesion: The inter-ministerial Structural Funds Working Group operates since March 1998 to improve the co-ordination of different activities in the preparatory process for work with the Structural Funds. The Structural Funds Co-ordination Division (established in May 1998) within the Foreign Assistance Programmes Co-ordination Directorate takes the role of the *Central Co-ordination Unit (CCU)* for the Special Preparatory Programme for the Structural Funds in Latvia (SPP) and, at the working level, implements the leading role of the National Aid Co-ordinator for the preparation process for the Structural Funds in Latvia.

The Rural Development Division was established under the Department of Agricultural Strategy and Co-operation in the Ministry of Agriculture in December 1998. The Division facilitates formulation, control and strategic guidance of the rural development policy, as well as co-ordination of elaboration of the SAPARD Rural Development Plan. Reform of 26 district departments of agriculture is under preparation.

The Rural Structural Program's Agency was founded in late 1998. This will be the main implementing institution for SAPARD from 2000.

Formation of planning regions is continuing and establishment of the Regional Development Agencies was started in 1999.

The Regional Development Council ensures co-ordination between ministries on regional policy issues. Its specific tasks include the design of Latvia's Regional Development strategy, consultations on draft regional development programmes and responsibility for the Regional Fund (support to specially assisted regions). Latvia continues to strengthen its institutions responsible for regional policy and cohesion.

Environment: The number of employees in the main co-ordinating structure of European Integration in the Ministry of Environmental Protection and Regional Development (MEPRD) - the European Integration Unit - has been increased from 3 to 7 at the beginning of 1999. Co-operation with other involved ministries is improving due to the work of the European Integration Working groups, which have been established in the main sectors of environmental legislation.

For management of programming, co-ordination and implementation of Pre-structural Funds assistance, the EU Financing Unit (4 employees) has been established. The State Environment Impact Assessment Bureau was established in January 1999 to ensure full implementation of EIA legislation. For the institutional strengthening of the Municipal Solid Waste Management (MSWM) system, in the beginning of 1999 a Project Implementation Unit was formed under the umbrella of the project implementation agency state non-profit organisation "Environmental projects", which is supervised by the Ministry of Environmental Protection and Regional Development.

A central Project Support Unit (PSU), under the umbrella of the state-owned non-profit organisation "Environmental Projects", was established to assist municipalities in carrying out projects. It works in close co-operation with the Ministry of Environmental Protection and Regional Development and Regional Environmental Boards and develops further activities within the defined project framework. It is planned to establish regional units for project co-ordination in 1999.

The working group on assessment of institutional capacities of the subordinated institutions to the MEPRD has been established. It has been concluded that there is no immediate need for reorganisation of Regional Boards, however, some clarification between the responsibilities of the Regional Boards and State Environmental inspectorate will be considered.

The final decision on the establishment of the Environmental Protection Agency (EPA) depends on the adoption of the framework law “*On Executive Agencies*” expected in late 1999 or beginning of 2000. Nevertheless, the structural reorganisation of subordinated institutions of MEPRD will be carried out by the end of 1999 to establish a joint institution capable of carrying out the functions of the Environmental Protection Agency, as well as new functions according to EU legislation.

Financial Control: The State Audit Office, an independent collegiate institution, is the central institution of the Latvian system for monitoring the use of state and local government budgets. 173 people, of whom 120 are auditors, were employed by the State Audit Office as at January 1999.

The SAO can request the dismissal of public servants responsible for losses to the state budget. During an audit, the State Audit Office assesses the work of internal control structures and delivers recommendations on necessary improvements. A total of 250 audits and 72 topical checks were performed in 1998, 257 audits and 14 topical checks are envisaged for 1999 including checks of utilisation of EU funds. Further strengthening of the SAO is envisaged. Each Ministry will set up an internal audit department functionally independent of the Ministry. The new Internal Audit units within the Ministries will be established using the existing Revision Units as the initial basis for their staffing. The Head of Internal Audit will report to the State Secretary of the Ministry in question, Ministry of Finance and State Audit Office. The internal audit system will be co-ordinated by the Ministry of Finance in accordance with the new internal audit regulations to be adopted in 1999.

4.3 Twinning

Latvia is actively participating in twinning under the PHARE programme. Since March 1998, the Public Administration Reform Bureau is placed in the centre of the Institution Building process to co-ordinate twinning projects between the EU Member States and Latvian administration. The director of the Public Administration Reform Bureau was appointed a National Contact Point for institution building and twinning in March 1998. The National Contact Point represents the Latvian administration within the network of National Contact Points, works with the EU in the twinning process, ensures a liaison with the EU administrations and also ensures the flow of information through the network.

Special attention is given to projects in four priority areas: Finance, Agriculture, Environment and Justice and Home Affairs.

In the PHARE '98 framework, there are six first-round twinning projects. Technical covenants for all these projects have been conditionally approved by the Twinning Steering Committee. Moreover, a technical covenant for the project “Institutional Strengthening of Latvian Environmental Administration for Implementation and Enforcement of EU Environmental Legislation (dealing with Water directives)” has been endorsed by the European Commission Delegation in Latvia. It will be ready for implementation in early September 1999.

Furthermore, in the framework of PHARE '98, there are two second-round twinning projects, both dealing with the Special Preparatory Programme: Technical assistance for the elaboration of the National Development Plan and Technical assistance for the elaboration of the Urban Development Pilot Programme. The respective beneficiaries are the Ministry of Finance and the Ministry of Environmental Protection and Regional Development. The Latvian side considered the twinning offers for the National Development Plan on 22 January 1999 and Urban Development Pilot Project on 25 February 1999. The Finnish offers by the Ministry of Interior were selected in both instances. In April and May kick-off meetings were organised to facilitate

elaboration of technical covenants between Finnish and Latvian twinning partners. At this stage the request for merger of these projects was lodged with the intention to exploit potential synergy effects.

In the PHARE '99 framework, three twinning projects are envisaged comprising projects on sustainable law approximation, with beneficiaries being the European Integration Bureau, the Saeima and line ministries; raising efficiency and effectiveness of human resource management within the State Revenue Service and reinforcing food control system at national and regional levels under the Ministry of Welfare. Twinning fiches for these projects were submitted to the European Commission at the end of March 1999. The deadline for submission of twinning proposals by the Member States was 25 June 1999. Twinning partner selection meetings are preliminarily scheduled for the first week of September 1999.

4.4 General evaluation

The medium term reform of public administration ensures that administrative structures able to apply and to enforce the *acquis* are in place. Structural reforms of public administration are occurring in accordance with the public administration reform strategy. Recognising the need to develop and improve administrative capacity in general, Latvia has assigned priority to key internal market areas such as standards and certification, financial services, anti-trust and state aid and customs and tax administration. Latvia continues to strengthen its institutions responsible for regional policy and cohesion. The training programmes for regional environmental authorities are under way and will be continued. The financial control mechanism is being strengthened. Latvia is beginning to develop a consumer protection policy and establishing the necessary institutions in the field of consumer protection. Latvia has established the necessary institutional infrastructure in the field of free movement of goods. Substantial efforts are continuing to strengthen enforcement capacity in the intellectual and industrial property area. Latvia is strengthening co-ordination of EU accession related work within the Ministry for Agriculture, for training in EU law and for additional resources to be allocated to the legal approximation process, in particular as regards veterinary, phytosanitary and food control areas. Latvia is making preparations for managing and properly controlling EU funds in the agriculture and food sectors.

C. ACCESSION PARTNERSHIP AND NATIONAL PROGRAMMES FOR THE ADOPTION OF THE ACQUIS: GLOBAL ASSESSMENT OF IMPLEMENTATION

1. Accession Partnership

the Accession Partnership is a single framework document where the priority areas for further pre-accession preparations are identified. Priorities, as set out in the Accession Partnership, are implemented through the Latvian National Programme for Integration into the European Union. It also incorporates the requirement for the National Programme for the Adoption of Acquis. Implementation of the short to medium term priorities of the Accession partnership has been successful. Detailed reports of that were provided to the European Commission and member states on two occasions: the second meeting of the Latvia and EU Association Council on 22 February 1999, and the second meeting of the Latvia and EU Association Committee on 16 June 1999.

Significant progress has been made in meeting the priorities set out in the Accession Partnership. This can be summarised as follows:

Political criteria

Latvia fully meets the first Copenhagen criteria. Protection of human rights has been reinforced with the adoption of the Chapter “Fundamental Human Rights” in the Constitution (*Satversme*). The naturalisation procedure has been simplified and improved. All non-citizens resident may now apply for citizenship and stateless children are eligible to receive citizenship automatically. Since changes to the “*Citizenship Law*” entered into force on 10 November 1998, the number for applications for naturalisation has increased significantly. The “*National Programme for Latvian Language Training*” is being implemented effectively. The naturalisation fee has been reduced and the number of questions for the naturalisation test of Latvian history has been reduced by a third. A new Information Centre dealing with naturalisation questions has been established. A National Programme for Integration of Society is under preparation.

Economic reform

Latvia has adopted a comprehensive medium-term economic strategy and a joint assessment with the European Commission has been carried out. The privatisation process is almost complete (95%) and at present the private sector accounts for 64% of GDP and employs 69% of the workforce. Strategies for areas where privatisation remains to be completed fully, such as public utilities, have been elaborated. Enterprise restructuring continues to be a priority. The banking sector is continuously being strengthened and is able to fulfil its role as a financial intermediary. The agricultural sector is being modernised, with 80% of agricultural land now privatised. Implementation of the veterinary and phytosanitary acquis, as well as restructuring of the food processing industry, is well advanced. The Land Register was upgraded and fulfils its role.

Internal Market Considerable progress has been achieved in the area of free movement of goods, especially as regards standards and conformity assessment. Significant steps have been made to fully meet EU requirements in the area of public procurement. In the area of intellectual property rights, a new law “*On Copyright and Associated Rights*” is to be adopted. Banking supervision activity of the Bank of Latvia has increased and is of a high quality. The Latvian insurance sector continues to be strengthened and was not disturbed by the recent events in Russia. The legal base for insurance operations was further refined. Latvia has adopted state aid legislation in line with EU law. A comprehensive and up-to date state aid inventory is in place. In the area of anti-trust

legislation, most of the legislation has been adopted pursuant to the new “*Competition Law*”. Major reform of excise tax legislation was accomplished with new laws *On Excise Tax for Tobacco Products* and *On Excise Tax for Alcoholic Beverages* coming into force. Administrative capacity has been improved in the area of tax and customs administration.

Justice and Home Affairs

The judicial system is being brought more closely in line with European standards as a result of several important developments. These include accelerated training for judges and bailiffs, an increase in the basic salary for judges, and creation of a Disciplinary Board to evaluate the work of judges. There has been a considerable decrease in procedural delays since the implementation of court system reforms. In the fight against organised crime and corruption, all the necessary legal and institutional instruments have been put in place. Asylum legislation in its main provisions corresponds to EU requirements. Substantial state funding was allocated to strengthening of Latvia’s eastern border. The demarcation of the land border is proceeding and infrastructure is being improved. Reform of the prison system continues to be a Government priority. In one fifth of prisons, reconstruction works are completed.

Environment

Latvia continues to make progress in this area. Detailed implementation programmes for all environmental sectors have been developed. Areas where progress in transposing EU environmental acquis is especially noticeable are air quality, water contamination, waste management and reduction of industrial pollution.

Reinforcement of institutional and administrative capacity

Latvia continues to increase the institutional and administrative capacity of its central and local administration. Public administration reform takes fully into account the need for applying and enforcing the acquis effectively. An institution building plan is now part of the Latvian NPAA and wider structural reforms of public administration are occurring as foreseen in the public administration reform strategy adopted in March 1998. Areas where progress in strengthening administrative capacity has been emphasised are the following: customs and tax administration, establishment of a tax payers register, establishment of Financial Police, social insurance, SRS system, management and personnel policies, competition, training of civil servants in EU affairs. Latvia also continues to strengthen institutions in the area of regional policy and cohesion.

2. National Programme for the Adoption of the Acquis

The III Latvian National Programme for Integration into the European Union was approved by the Government in 1998. This programme, which incorporates the requirement for a National Programme for Adoption of the Acquis, was considered by the European Commission in its 1998 Regular Progress Report, and its comments have been taken into consideration in the revision.

The comments on the structure and content of the III National Programme were positive and encouraging. The Commission stated that the Programme represented a good start for setting priorities on how to assume the obligations of EU membership. Following further dialogue with the Commission on the structure of the National Programme, and taking into account the guidance provided by the Commission (February 1999) on harmonisation of the scope and structure to ensure that all aspects of membership preparations are covered, a comprehensive revision of the National Programme was carried out.

This is the first revision of the National Programme in the context of the EU reinforced pre-accession strategy. The Latvian administration has chosen to continue to use the title “*National Programme for Integration into the EU*”, because the National programme will have increasing

public significance in Latvia's membership preparations and this title is more meaningful in such a context.

The thrust of the present Programme derives essentially from a more focused and integrated response to the challenge of accession as set out in the Opinion and the 1998 Regular Report, as well as in the Accession Partnership document. The dialogue with the Commission on the preparation of the National Programme has helped to consolidate the framework within which European integration policy is conceived, formulated and developed.

As with the Third National Programme, the **structure** followed is essentially similar to that of the Commission's Opinion and the Regular Progress Reports. The wider **scope** of the revised National Programme includes:

- Expanded coverage of the Accession Partnership priorities in specific areas, including fuller reference to the relevant *acquis* and all specific directives within individual Technical Fiches;
- New issues arising from the commencement of the bilateral screening process and discussions in the context of the Europe Agreement, including the sharper focus that this has brought to the work of adopting the *acquis*;
- Revised and consistently structured Technical Fiches set out more clearly the objectives and the planned activities for their achievement. This revised structure has ensured a greater realism and coherence in the descriptions and timings of specific projects and allows increased national capacities to monitor and assess progress in this area. A clearer distinction is made between activities for law approximation and institution building;
- The revised National Programme is covering the *acquis* to a much greater extent. Each Technical Fiche makes reference to all relevant directives, ensuring that the full *acquis* is identified and that there are no gaps. This will also allow the necessary preparatory work to be identified and planned over a defined time frame.

The form of the National Programme is that of a dynamic and essentially practical instrument, allowing for regular changes to be made to the Technical Fiches and sectoral priority areas, as and when they occur. These can include changes to reform priorities arising from national reflection and/or dialogue with the EU and the European Commission. This will ensure that the programme is a **living instrument** that can adapt to changes in the pre-accession process.

It is anticipated that the National Programme will facilitate ongoing monitoring of the adoption and implementation of the *acquis* within Latvia by providing an internal instrument for co-ordination and monitoring; it will provide a basis for including new actions arising from the screening exercise and the outcome of discussions in the institutions of the Europe Agreement. In addition, it will allow for easier, more structured and transparent preparation of the Commission's Regular Progress Reports. This means that the National programme represents a **single and coherent national management framework** for planning, prioritising, delivering and monitoring Latvia's accession preparations in the different sectors.

Key issues for the Fourth National Programme for Integration into the EU

Coverage of the Acquis

The National Programme covers every area of the *acquis*. In most cases it has been both appropriate and possible to identify deadlines by which specific pieces of EU legislation will be transposed into Latvian laws. The results of the current screening exercise have added a sharper

perspective to the work to be achieved in adopting the *acquis*. In some cases, new areas have emerged as priorities for the approximation process. In others, work previously considered completed may now feature as one for further development and elaboration.

Coherence with National Budget – Financial Programming

One of the key principles underpinning the design and formulation of the Fourth National Programme is that of budgetary realism. In preparing the Programme every effort has been made to ensure that only those actions for which financial commitments are secured in the National Budget will be carried into the financial programming of the NPEI/NPAA. Significant measures are being taken to ensure a close alignment between the National Budget and the NPEI/NPAA in so far as the financing of all activities is concerned.

A separate chapter of the Programme covers the financial implications from implementing membership preparations in the short and medium term. The corresponding financing sources, i.e. the national budget, PHARE, ISPA, SAPARD and bilateral assistance are set out in the financial tables for the period from 1999 to 2000. Information covered will be constantly updated. The Ministry of Finance has undertaken a substantial amount of joint work with the European Integration Bureau to ensure, as far as possible, coherence of the financial aspects of the National programme with budgetary resources.

A Single National Framework

The Fourth National Programme provides a single national framework for planning, prioritising and monitoring the accession process in its different sectors. It brings together in a single document the priorities for implementing the *acquis* along with an indication of development/investment priorities.

The revised structure of the National programme allows planned investments to be taken into account in the year 2000 and beyond. This means that it will anticipate future support under ISPA, SAPARD and PHARE, all of which are pre-conditioned by the Accession Partnership. Given that each of the sectors eligible for ISPA and SAPARD funding will be preparing national programmes (agriculture and rural development, transport and environment), the references in the NPEI/NPAA will be at the strategic rather than at detailed action level.

Coherence with the Institution Building Plan

Following a suggestion by the European Commission, an Institution Building Plan was elaborated as an integrated chapter of the National Programme for Adoption of *Acquis*. The Institution Building Plan effectively is a summary of institution building measures listed under various *acquis* sectors included into the NPAA and reflects priorities set by both the government and the European Commission. The plan will be an important instrument for strengthening of the administrative capacity (e.g. in dealing with strategic and analytical issues), and should provide a basis for the PHARE institution building/twinning programme. The Fourth National Programme represents an appropriate single framework for managing the pre-accession process. The National Programme mechanism will enable the Latvian authorities to manage the legal, institutional and organisational changes that are fundamental to the accession preparations and to oversee progress in relation to the wider aspects of the integration process.