

**The Road to Democratization and Self-sustainability in Bosnia
and Herzegovina:**

The Case of the Value Added Tax Law (2005)

By

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INTRODUCTION

The General Framework Agreement for Peace in Bosnia and Herzegovina, otherwise known as the Dayton agreement, ended nearly four years of armed conflict in that country, and engaged the international community¹ in one of the most ambitious rebuilding and democratization processes since the Marshall Plan. Nearly twelve years since its signing in December of 1995, after tens of thousands of invested work-hours by the world's top international administrators, and billions of Euros in reconstruction aid, Bosnia and Herzegovina, though seemingly far from the chance of returning to the armed conflict of its recent history, is by no measure a stable and self-sustainable country, politically or economically speaking. As the mandate of its civil international administrator, the Office of the High Representative (OHR) winds down with its announced end-date in June of 2008, the question of the ultimate success or failure of Dayton and, indeed, Bosnia, is very much a timely one.

The return of strongly nationalistic rhetoric by Bosnia²'s politicians in the run up to, and the aftermath of the October 2006 elections, was only one of the worrying signs of a deteriorating political situation. Process of Bosnia's European integration, to be officially started by the signing of the Stabilisation and Association Agreement (SAA) with the European Union, has been indeterminately delayed due to the lack of agreement on police reform between main political parties. The current Council of Ministers, Bosnia's state-level executive body, created after months of delay due to post-elections coalition-making, has been mired in inter-ethnic power-plays between its ministers, and has passed on to the Parliament no significant legislation thus far³. Milorad Dodik, the Prime Minister of Republika Srpska (RS), and the head of the leading RS party, SNSD, has recently noted that he will

¹ A loose, informal term meant to encompass the multiple international actors in Bosnia, from the Office of the High Representative, to the EU, US and other governments, onto numerous NGOs and international organizations such as the World Bank, and IMF.

² Term Bosnia will be used in the paper, for purely stylistic purposes, to denote the full name of the country, namely Bosnia and Herzegovina.

³ Terzic, April 2007.

support efforts to roll back the transfer of competencies from the entity level to the state level achieved over the past ten years⁴, thus effectively weakening the state-level institutions and injecting a fresh dose of uncertainty about Bosnia's future.

As mentioned, all these recent developments are happening under the expectation that OHR will close its doors in a year's time, taking with it the legislative and executive powers (the so-called Bonn Powers) that were instrumental to creating much of the hard-won progress that happened in Bosnia over the past decade. When OHR steps back, the Special Representative for the EU is supposed to step in, enticingly offering the prospect of EU membership to Bosnia's fragmented political elites, and hoping that the pull of economic prosperity and European membership will be strong enough to win out over centrifugal nationalistic policies. The results thus far are not encouraging.

That Bosnia is still *not* a self-sustainable country, either politically or economically, is not in question. *Why* Bosnia is still not a self-sustainable country, after more than a decade of peacetime, billions of hard currency in reconstruction aid, and outward trappings of democracy (frequent elections, free press, etc.), has been a subject of many academic works in the past decade. There seem to be as many culprits for the current situation as there are people analyzing it, but three main factors have been identified as the main roadblocks toward full democratization, economic stabilization, and European integration of Bosnia.

One is Dayton itself, namely the institutional set-up stemming directly from it; weak, nearly ineffective central government and strong, autonomous entities, as well as the complex, multi-layer power-sharing system of government that it brought with it⁵. The other is quite obvious – the deep, lasting ethno-political divisions within the country, maintained and abused by obstructionist and self-serving nationalistic politicians⁶, are making any moves towards political, social and economic reintegration highly difficult. Last, but not least, is the effect of the international administration in

⁴ OHR, May 2007.

⁵ For complexities of Dayton, see International Crisis Group (1999), Bose (2002), Bieber (2005), among others.

⁶ European Stability Initiative, October, 1999.

Bosnia⁷; it has been argued that OHR's use of its decision-making power (useful or not, necessary or not) did have a negative impact on the development of politically-savvy, accountable local politicians who were aware of, and ready to tackle difficult political decisions. This kind of “short-circuiting” of the decision-making process by the High Representative was seen as having deprived BH politicians of the chance to be able to face and make difficult decisions and learn the ‘culture’ of political compromise. It has also allowed elected officials to avoid accountability, as they have grown used to the strong hand of OHR coming down from above to impose decisions, allowing them to go back to their constituents and blame the international community for decisions that could be politically risky for them personally.

Every political and economic failure and setback in the past twelve years can be explained in terms of the influence of one of these three factors, or any combination thereof. Be it cumbersome bureaucracy, non-functioning governmental bodies, stalled privatization, fractured economic market, high unemployment, failed constitutional changes – the core reason for lack of progress or outright failure is either the institutional gridlock created by Dayton, too much (or too little) interference by the OHR, or plain old obstructionism by self-serving nationalistic politicians.

It has been the goal of the international community in Bosnia to set the country on a firm and irreversible path to the European Union. This would seem to be the one goal that would ensure the continued, successful and peaceful existence of Bosnia and prosperity for its peoples. This goal, however, cannot be achieved with the OHR at the helm, directing the course and keeping obstinate politicians in line – it has to be achieved from within, designed and implemented by Bosnian politicians working together to set Bosnia on the course for the EU. In order to ensure Bosnia's viability as a stable, self-sustainable democracy, local elites must prove that the political will, ability to compromise, and the know-how needed to bring Bosnia closer to European integration exist. To this purpose, the path OHR took was to ensure that the majority of laws brought before the Bosnian

⁷ For some of the most scathing commentary, see Chandler (2000), Knaus and Felix (2003).

Parliament and argued there, and hopefully passed, do bear the mark of 'Made in Bosnia', rather than 'Made by the OHR'. To achieve this, especially in the view of the announced closing of OHR in June of 2008 and the likely loss of its use of the 'Bonn Powers' to impose laws and decisions, the tactic has been to provide needed legal expertise, and prod the Bosnian politicians from behind the scenes, but ultimately leave it up to them to argue the points of each proposal and bear the consequences of their actions in public.

Given this brief background both on the main factors affecting Bosnia's path to achieving self-sustainable status, the aim of this work will be to analyze their impact on the decision-making process in Bosnia and Herzegovina, as exemplified through the legislative process surrounding the 2005 Law on VAT, a law that enabled Bosnia to take “a great step forward⁸” in its quest for European integration. I believe this type of case study analysis will help us go beyond the general academic prototyping, by allowing us to concretely apply these grand theories of what is wrong with Bosnia’s system of governance to an example of decision-making that involved both local and international actors. Was this particular example considered a success because the three factors have *not* had a strong effect on the process, or *despite* their impact?

In order to approach the analysis, in the first section I will need to explain the constitutional and institutional set up of Bosnia and Herzegovina, as laid out by Dayton. I will aim to delineate the complexities of the consociational system as in effect in Bosnia, with its multiple, cascading levels of government, ethnic representation, complex decision-making processes, and the role of the international actors within the country.

After the governance system in Bosnia is explored, I will be able to, in the next section, describe the direct effects each of the three factors, namely Dayton's institutional set-up, effects of international administration, and nationalist politics, have had on the democratic development and self-

⁸ Finance Deputy Minister Jusuf Kumalic, unauthorized transcript of the 43. session of the House of Representatives held on September 8, 2004.

sustainability of the country.

In the following section I will seek to directly analyze how the decision-process during the legislative deliberation on the 2005 Law on VAT in Bosnia was affected, either positively or negatively, by each of the three factors.

BACKGROUND TO THE CONFLICT

The War

A detailed discussion of the three and a half year war in Bosnia is not possible, nor necessarily needed, in the framework of this work⁹. Instead, I will offer a brief outline of the main developments, with the purpose of highlighting the depth of post-war divisions in Bosnia.

Bosnia, until its 1992 independence referendum and subsequent international recognition, was one of the six republics within the Socialist Federative Republic of Yugoslavia. Bosnia was both one of the least economically prosperous and most ethnically diverse republics in Yugoslavia, and the League of Communists of Bosnia and Herzegovina was one of the most dogmatic and strict ones within Yugoslavia.

Bosnian population, according to the 1991 census¹⁰, was constituted of the three main groups – Muslims¹¹, Serbs and Croats – which together made up 92.1 percent of the total population, with another 5.6 percent having declared themselves as Yugoslavs. The remaining 2 percent of the population belonged to a number of smaller groups, including Jews and the Roma. According to the

⁹ For an in-depth look at the Yugoslav conflict in general, and Bosnia specifically, consult “Yugoslavia: Death of a Nation” by Laura Silber and Allan Little, and “Bosnia: A Short History” by Noel Malcom.

¹⁰ The census data was obtained from the Federal Office of Statistics of the Federation of Bosnia and Herzegovina (<http://www.fzs.ba/Eng/index.htm>).

¹¹ The term Muslim was, at a congress of Muslim intellectuals in 1993, replaced by a more religion-neutral term Bosniac. I shall use the two terms interchangeably, depending on the time period in question: Muslim for the war and pre-war period, Bosniac for the post-war times.

census, Muslims constituted 43.5 percent of the total population of 4.3 million inhabitants, Serbs 31.2 percent, and Croats 17.4 percent. It has been argued that ethnic heterogeneity, low level of economic development and the rigidity of the communist system all had a role to play in the conflict that ensued, but the cancer of the region is admittedly the virulent nationalism that engulfed the area in the early nineties.

The short summary of the major developments during war-time in Bosnia is as follows: The first multi-party elections in Bosnia took place at the end of 1990, following the trend in Croatia and Slovenia, and the rest of Eastern and Central Europe. Three main nationalist, mono-ethnic parties emerged on the scene in Bosnia – the Party of Democratic Action (Stranka Demokratske Akcije, SDA), a Muslim party; Serb Democratic Party (Srpska Demokratska Stranka, SDS), and Croat Democratic Community (Hrvatska Demokratska Zajednica, HDZ). The three nationalist parties won 71 percent of the vote, and the seat distribution in the parliament largely followed the ethnic composition of the populace, with SDA controlling 35.9 percent of the parliamentary seats, SDS 30 percent and HDZ 18.4 percent. The remainder of the seats, a mere 15 percent, went to the multiethnic, non-nationalist parties.¹² The wide power-sharing arrangement established by the three nationalist parties after the elections quickly broke down as each of the parties focused on representing the narrow, and often diametrically opposed, interests of their own ethnic group. This caused the Bosnian society at large to grow polarized and “politics degenerated into a zero-sum game”.¹³ The ruling parties could not agree on the most basic governing principles – no constitution was drafted, and there was no consensus as to the shape of the political system – proponents of territorial decentralization argued against proponents of centralized power-sharing.¹⁴

Meanwhile, Yugoslavia was disintegrating. Slovenia and Croatia were pushing for full independence within their own polarized national environments, which they unilaterally declared in

¹² Bieber, 2005, p. 21.

¹³ International Crisis Group, Europe Report No 42, 1998.

¹⁴ Bieber, 2005, p. 24.

June of 1991. Separatist Serb minority leaders in Croatia in turn declared independence of a Serb Republic of Krajina from the Republic of Croatia, and Croatia descended into armed fighting.

Influenced by the separatist actions of the Serb minority in the neighboring Croatia, and the escalating conflict there, Bosnian Serb leadership declared a number of Serb Autonomous Areas within Bosnia, with the goal of secession and eventual unification with Serbia.

Full-on armed conflict in Bosnia began after the independence referendum organized in March of 1992, which was boycotted by the Serb population, and the subsequent declaration of independence of Bosnia. The capital, Sarajevo, was besieged by Bosnian Serb forces and the Yugoslav National Army, and an offensive was launched in Eastern and Northwestern Bosnia with the aim of territorial consolidation of the Serb-controlled areas. Due to the high ethnic heterogeneity of the population in Bosnia¹⁵, these moves were followed by a massive campaign of ethnic cleansing of the non-Serb population, using tactics such as mass murder, expulsion and destruction of property of Muslims and Croats.

By mid-1993, the fragile Muslim-Croat alliance fell prey to the growing separatism of the hard-line Croatian nationalists, wanting to separate Western Herzegovina from Bosnia and join it with Croatia, and the alliance devolved into a severe armed conflict. Thus, by the end of 1993, nearly seventy percent of the Bosnian territory was held by the Serb forces, and the remaining thirty percent was being fought over by Croats and Muslims. In 1994, under severe pressure from the United States of America, the Croat and Muslim sides entered a cease-fire agreement which resulted in the creation of a Muslim-Croat Federation, and a joint strategy against the Bosnian Serb army.

The overall conflict ended in 1995 with the signing of the Dayton Peace Agreement in November of that year. The agreement was preceded by joint Croatian/Bosnian Army movements that recaptured large areas held by the Serbs, and NATO bombardment of the Bosnian Serb army positions.

¹⁵ Please consult Map 1 (included in the Appendix) for a visual of territorial heterogeneity of different nationalities in Bosnia.

This leveled the playing field some, and the Dayton agreement mainly followed the territorial demarcation line between the warring parties at the time of signing. At the end of 1995, a new Bosnia emerged, one consisting of two political entities, the Bosniac-Croat Federation of Bosnia and Herzegovina, and the Serb Republika Srpska (Serb Republic), covering 51 and 49 percent of the total territory of Bosnia, respectively. Though Bosnia was nominatively still a unified country consisting of three constitutive nations, war-time crimes and ethnic cleansing left deep scars in both the territorial reality of the country, and the national consciousness of all three ethnicities.

Consociationalism: Theory

Power-sharing, defined as “practices and institutions that result in broad-based governing coalitions generally inclusive of all major ethnic groups in society,”¹⁶ has emerged as the leading institutional-building approach to managing ethnic conflict through democratic practices. There are two main approaches to constructing democracy in deeply divided societies – the consociational, or 'group building-block' approach, that relies on ethnically homogeneous groups (mainly political parties) to cooperate together and form 'building-blocks' of civil society, and this approach relies on a high level of group autonomy; and the integrative, or pluralist, approach, that emphasizes political alliances across ethnic lines as an incentive for moderation among political leaders – this approach relies on pre-election pacts among political parties across ethnic lines.¹⁷

One of the main proponents of the 'group building-block' approach to bridging the ethnic rift in a multinational society is Arend Lijphart, a professor of politics at the University of California. It was Lijphart who first formulated the concept of consociationalism as a power-sharing model of government between the ethnic elites in a plural society, a concept whose main goals are avoidance of

¹⁶ Sisk, in *Democracy and Deep-Rooted Conflict: Options for Negotiators*, 1996, p. vii.

¹⁷ Sisk, 1996, p. 144.

violent conflict and the survival and strengthening of democracy. Per Lijphart, the main attributes of a consociational system are (1) executive power-sharing (grand coalition) between different groups, (2) group autonomy, (3) proportionality and (4) mutual veto.¹⁸ This kind of governmental organization was constitutionalized in Bosnia on all levels of government, with the 1995 Dayton¹⁹ peace agreements, in hopes of stopping armed conflict and transforming it into a democratic process of political competition, with the end result of creating a stable, multiethnic democratic state. That the armed conflict has been transformed into a protracted, though peaceful, bout of political arm-wrestling between the elites of the three nationalities in Bosnia is clear, but so are the deficiencies of Dayton as a long-term basis for economic development and democratization of the country.

Power-sharing is seen by many policymakers and scholars as the essential element to successfully managing ethnic conflicts in divided societies, as it employs “on-going, nonviolent bargaining by peoples who share a common state”²⁰ as a means of managing intergroup disputes through, not armed conflict. Though there is disagreement between scholars as to whether the consociational or the integrative approach leads to better conflict management, I will focus solely on the consociationalism, as that was the power-sharing module employed in Bosnia.

Consociationalism, as explained earlier, has four main attributes – two primary, and two secondary ones – that enable it, per Lijphart, to promulgate the creation of a successful democracy in divided societies. The primary attributes are sharing of executive power and group autonomy. Power-sharing, or a grand coalition, ensures the participation of the leaders of all significant segments of the society through post-election coalition-building, thus preventing permanent exclusion of a minority from power. The main achievement of the grand coalitions is that decisions are reached through

¹⁸ Lijphart, 1968, 1977.

¹⁹ The full name of the agreement, which was brokered in Dayton, Ohio, is the General Framework Agreement for Peace in Bosnia and Herzegovina, but I will be mostly referring to it as the Dayton agreement, or the Dayton accords in the paper.

²⁰ Sisk, 1996, p.4.

consensus of political elites of all the significant segments of the society.²¹

Group autonomy, whether territorial or non-territorial, ensures minority-rule “over itself in the area of the minority's exclusive concern” through the devaluation of decision-making power from a central authority to that of minority groups. This concept mirrors the European Union's concept of subsidiarity, where decisions on matters of common interest (environmental policy, indirect taxation, international trade, monetary policy) are made centrally, through consensus of the representatives of all the segments of the society, but decisions on other matters (culture, education, local rule) should be devolved to the minorities, or the local levels. This devolution of authority to the segments of the society can take a territorial form (federalism), or non-territorial form (cultural autonomy, for instance)²².

One of the two secondary ingredients of consociationalism that help strengthen the primary characteristics is proportionality. Proportionality in consociationalism serves two functions: In the decision-making process it ensures not only that all significant segments of the society are represented in decision-making organs, but also that they are represented proportionately; in the administrative arena (on the central, regional and local level) it ensures proportional distribution of jobs and resources, precluding any minority being discriminated against²³.

Minority, or mutual veto, on the other hand, offsets the possibility of a minority being outvoted in a grand-coalition, and provides each segment of the society with “a guarantee that it will not be out voted by the majority when its vital interests are at stake.”²⁴ Minority veto gives the much-needed assurance to each of the groups involved in the ethnic conflict that they will be able to protect itself from possible adversarial decisions of a grand-coalition majority²⁵.

With these four attributes, consociationalism, in theory, seems to offer plentiful assurances to

²¹ Lijphart, 1977, p. 31-36.

²² Ibid., p. 41-44

²³ Ibid., p.38-41.

²⁴ Lijphart, as quoted in Sisk, *Power Sharing and International Mediation in Ethnic Conflicts*, p. 36.

²⁵ Lijphart, 1977, p.36-38.

the warring groups that their vital interests and decision-making powers will be protected and assured in a country in which they form a minority, thus paving a way for ethnic reconciliation and consolidated democratic rule. How well these concepts work on the ground will be seen when we look at the case of Bosnia, where a consociational democracy has been engineered by the international community more than ten years ago.

Consociationalism: The Case of Bosnia and Herzegovina

As a result of the 1992-1995 war and the Dayton accords, Bosnia is defined as a *de facto* federal state with a weak central government, and two highly autonomous political “entities”: the Federation of Bosnia and Herzegovina (Federation), holding 51 percent of the territory, itself separated into ten cantons, and Republika Srpska, with 49 percent of the territory. The status of the Brcko municipality in northeast Bosnia has been disputed by both entities, and, after several years of international arbitration, has been given separate status in 2000 as a district separate from either entity (along the lines of the District of Columbia in the US). Dayton has also conferred upon the three main ethnic groups – Bosniacs, Serbs and Croats²⁶ - the status of constituent peoples.

Bosnia's government structure is also regulated by Dayton and is highly complex – and arguably unworkable. There are multiple levels of power – on the state, entity, cantonal, and municipal level. The significant role of the international community in the running of the country, enshrined in the Dayton accords, has made Bosnia a *de facto* protectorate, and power of the central government is further diluted by the federal arrangement of the country, with established strong governments of the two entities. Each of the fourteen²⁷ political units in Bosnia has its own constitution and legislative powers, and is organized under a complex system of inter-ethnic power sharing, making the entire

²⁶ Bosnia's Constitution recognizes only Bosniacs, Serbs and Croats as constituent peoples. There is about a dozen other ethnic groups which are legally recognized as national minorities, and termed as “Others” in the Constitution.

²⁷ Central government, two entities, ten cantons, and the district of Brcko.

structure of governance of the country even more unmanageable. The governance system in Bosnia, as mentioned before, is based on power-sharing among the three major ethnic groups as delineated by Lijphart in his theory of consociationalism. As a 'group building-block' approach to the power-sharing system, Lijphart's consociationalism won over the integrative approach advocated by Horowitz²⁸, as the indelible reality of Bosnia at the time of the signing of Dayton and, quite certainly today, is that of deep ethnic divisions, thus making political alliances across ethnic lines, necessary for integrative system to work, untenable.

Bosnia's internal structure, as stipulated by Dayton, is nearly a text-book example of consociationalism. *Grand coalitions*, which include members from all three constituent nations, are needed to form a government on both the state and entity level. At the state level there are two parliamentary chambers and the entity quota is employed, ensuring that two-thirds of members have to be from the Federation and one third from Republika Srpska. Furthermore, each chamber will elect a Chair and two Deputy Chairs, one Bosniac, one Croat and one Serb, and the Chair position will rotate between them. The Council of Ministers (CoM) follows the same distribution key, and each of the ministers had to have two deputy ministers, one from each of the other two nations. This changed in 2003, at which time the position of the CoM Chairman was set for a term of office of four years, with no rotation between the Chairman and the co-chairs. The Presidency consists of three members and is based on both national and territorial basis – the Bosniac and Croat members can only be elected by the voters in the Federation, and the Serb member can only be elected by the voters in Republika Srpska. The chairmanship of the Presidency rotates every eight months, ensuring each of the members holds it during their two-year term.

At the entity level, in the Federation there have to be eight Bosniac ministers, five Croat ministers and three Serb ministers. In Republika Srpska, five ministers have to be Bosniac and three

²⁸ For Horowitz's theories on integrative power-sharing refer to Donald L. Horowitz *Ethnic Groups in Conflict* and "Constitutional Design: Proposals Versus Process" in *The Architecture of Democracy: Constitutional Design, Conflict Management, and Democracy*, ed. Andrew Reynolds.

Croat. Since 2002, the National Assembly in Republika Srpska must have at least four members from all nations, and in the Federation, the House of People had to have equal number of Bosniacs, Croats and Serbs – seventeen each.²⁹

In terms of *minority veto*, each of the three communities in Bosnia has the right to veto decisions of the Presidency, the Council of Ministers, and the parliament that are seen as having a negative effect on their community. This applies to the state, entity and, in Federation's case, cantonal level.

Proportional representation is achieved on the state level through equal representation of all three groups in the two chambers of the Parliament, regardless of their size as the percentage of entire population, and firm rules on the division of ruling posts according to the ethnic key. In terms of public administration is governed by the Civic Service Law, imposed by the OHR in 2002.³⁰ Per the law, the structure of civil servants within the civil service shall generally reflect the ethnic structure of the population of Bosnia and Herzegovina in accordance with the last census.³¹ This law, and its requirements, were also instituted on the entity level. This is especially important in terms of minority representation within the police forces of the two entities, but the legal requirements have thus far not been fully translated into success on the ground, especially in the case of Republika Srpska.³²

Segmental autonomy is achieved in territorial terms, on entity level in Bosnia, and furthermore on cantonal level within Federation.³³ Though not explicitly described as such in the Dayton accords, the constitutionalization of the entities after the war has effectively transformed Bosnia into a confederal state, one defined by a very weak central government and highly autonomous entity governments. I will analyze this set up in more depth in following sections.

²⁹ Bieber, 2005, p. 40-83.

³⁰ Bieber, 2005, p. 57.

³¹ Art.2, Law on Civil Service in the Institutions of Bosnia and Herzegovina, 23.05.2002. The last census in Bosnia was held in 1991 and reflects the pre-war, pre-ethnic cleansing population distribution.

³² Bieber, 2005, p.73-74 and p.81-83.

³³ Federation is composed of 10 cantons, eight of which are ethnically homogeneous – three predominantly Croat, and five Bosniac.

THREE FACTORS INFLUENCING DEMOCRATIZATION

THE DAYTON PEACE AGREEMENT

Consociationalism: A Valid Choice for Bosnia?

As mentioned earlier, there are three main factors that have a wide effect on the governance and development of democracy in Bosnia. The Dayton agreement, with its consociational institutionalization of power-sharing in Bosnia, the very backbone of the country's post-war existence, has been described, even by those sympathetic to its role, as unwieldy, too costly, and easily open to obstruction by nationalistic politicians. One of the more basic questions is – should a consociational system have been implemented in Bosnia in the first place?

Per Lijphart, there has to exist a number of factors which are conducive to power-sharing in order for the consociationalism to be effective. These factors are the following:

- Multiple balance of power;
- The total population is relatively small so that the decision-making process is less complex;
- There are external dangers that promote internal unity;
- There are overarching loyalties that reduce the strength of particularistic ethnic loyalties;
- The ethnic groups are geographically concentrated so that federalism can be used to promote group autonomy;
- There are prior traditions of compromise and accommodation.³⁴

Three of the preconditions exist – there is a multiple balance of power in Bosnia, in the sense that no ethnic group has a clear majority. Bosniacs, as a group with the plurality of the population,

³⁴ Lijphart, 1977, p. 53-103.

43.5 percent, can still be outvoted by a possible Croat/Serb coalition. The country is small enough, with the pre-war population numbering less than 4.5 million, but that does not translate into a less complex decision-making process in Bosnia's case. Lijphart envisioned small countries as not engaging in extensive foreign policy decisions, due to their limited influence, and possibly even maintaining neutrality, thus limiting the amount of internal discord. However, as enshrined in the Dayton agreement, the entities were given the right “to establish special parallel relationships with neighboring states consistent with the sovereignty and territorial integrity of Bosnia and Herzegovina³⁵,” and the Federation and Republika Srpska have promptly done so, signing agreements with Croatia and Serbia, respectively. Lastly, post-war population is indeed territorially homogeneous in a manner that makes (con)federalism possible, but this also makes the specter of secession all the more real.

Some of the crucial preconditions are notably absent – there are no external dangers that could promote internal unity; as a matter of fact, the 'enemies' to each of the groups come from within the state, and the perception of these threats is effectively abused by the nationalist party leaders. There are no prior traditions of compromise and accommodation – Bosnia was plunged into a fierce war after fifty years of one-party communist rule, and the only constructive collaborating done between the three main nationalist parties (SDA, HDZ and SDS) has been done in order to “prevent the passage of reforms that might undermine their ability to exploit ethno-nationalism to win elections.”³⁶ There is no successful multi-ethnic nation-wide party in Bosnia that could challenge the rule of the nationalist parties, despite the continued efforts of the international community to skew the electoral law in favor of moderate politicians³⁷. Last but not least, given the constitutional set-up of country that employs strict ethnic division of power, and the legacy of the 1992-1995 war, there exists no overarching sense

³⁵ Constitution of Bosnia and Herzegovina, Art.3, Part 2a.

³⁶ Manning, p.75.

³⁷ For more on electoral reform and party system in Bosnia, please refer to Chandler, D., *Bosnia: Faking Democracy After Dayton*, Bieber, F., *Post-War Bosnia: Ethnicity, Inequality and Public Sector Governance*, Manning, C., “Elections and Political Change in Post-War Bosnia and Herzegovina”, *Democratization*, Vol.11, No.2., among others.

of belonging in Bosnia that could reduce the strength of ethnic loyalty.

The fact that the preconditions for successful implementation of consociationalism do not exist in Bosnia is big enough of a problem. However, there are pointed critiques of consociationalism in general that bring in question its usefulness as an applicable theory. Steven Burg argues that consociationalism can be viewed as the “ultimate form of elite manipulation and control”, claiming that manipulation of latent nationalism and abuse of power-sharing and mutual veto can be used by political elites against the will of their electorates in order to paralyze governance and disrupt the state.³⁸ Burg uses examples of the dissolution of Czechoslovakia and Yugoslavia to illustrate his point, but his point can be directly tied to the example of Bosnia during 1991-1992, as well as in the post-war years. This sentiment is echoed by Horowitz, who says that “it is a mistake to impute good intentions to leaders without good political reasons for thinking they in fact entertain such intentions.”³⁹

The possibility that the very elites running the country have little to no interest in seeing it thrive as a consociational democracy is worrying, but reflects a too-often cynical and highly self-serving position of politicians on the ground. It is Lijphart who himself said that, “Consociational democracy entails the cooperation by segmental leaders in spite of the deep cleavages separating the segments. This requires that the leaders feel at least some commitment to the maintenance of the unity of the country as well as a commitment to democratic practices.”⁴⁰ This, in a country whose very symbols – flag, coat of arms and national anthem – have had to be imposed by the High Representative due to the inability of the leaders of the three national groups to agree on a unifying symbol, seems very far from achievable reality. The reality, bleakly enough, seems to point in a different direction: the leader of the indisputably strongest Croat party in Bosnia, the nationalist HDZ, and the Croat member of the Bosnian Presidency at the time, Ante Jelavic, unilaterally announced Croat withdrawal

³⁸ Personal communication between Steven Burg and Timothy Sisk, as quoted in Sisk, p.39.

³⁹ Horowitz, 1985, p.573-574.

⁴⁰ Lijphart, 1977, p. 53

from the joint Federation institutions and establishment of Croat self-government in March of 2001.⁴¹ Currently, the Prime Minister of Republika Srpska, Milorad Dodik, who has been seen as the acceptable 'moderate' candidate by the international players, has been calling for an independence referendum, and secession of Republika Srpska, and – having toned down that rhetoric slightly – for the rolling back of all the competencies that have been transferred from the Entity, onto the State level, including that of a new system of centralized revenue distribution, part of the VAT process.⁴²

Consociationalism also, according to its critics, has limited effectiveness in promoting long-term cooperation and inter-ethnic compromise. Furthermore, it may actually strengthen ethnic divisions, rather than ameliorate them. As Roberto Belloni notes :

“Ethnic quotas reinforced the salience of ethnic identity and cleavages, entrenched many of the ethnic divisions that international intervention was supposed to soften and eventually overcome, and risked perpetuating instability. Without incentives for cooperation, it has been easy for politicians to win popularity by defending their national group and by portraying others as enemies.”⁴³

This kind of strict institutionalization of ethnic divisions, where each group is guaranteed representation according to a set ethnic key, and has further reassurances, such as minority veto, is well suited as a policy that can help end armed conflict and help transform the warring parties into democracy-minded politicians. However, institutionalized ethnic division is not likely to prove a stable solution in the long run. A certain level of plasticity and fluidity is needed in order to be able to shape the consociational system according to the changing circumstances in the field.

Another critique of consociationalism, coming from Horowitz, is that consociationalism provides no incentives for moderate behavior. He argues that Lijphart's assumption that political leadership enjoys a high degree of freedom of choice and independence and has the ability to engage in consensus-making with opposition leaders is not true. Horowitz argues that political leadership of an

⁴¹ Bieber, 2005, p.65. In response to this move, Jelavic was removed from power and barred from politics by the High Representative, and Croat self-government failed due to strong opposition from the OHR and the government of the Federation, led by an alliance of moderate parties at that time.

⁴² See newspaper articles “Tihic džabe preti.” *Vecernje Novosti*, 27.08.2006; “Dodik: Pravo na referendum.” B92.net, 27.05.2006; “Dodik: Referendum u RS neizbezan.” *Blic on-line*, 04.09.2006. “Dodik: Slaba vajda od reformi.” *Blic on-line*, 05.05.2007. “OHR: Transfer of Competency Agreement Withdrawal Legally Questionable.” 08.05.2007.

⁴³ Roberto Belloni, “Peacebuilding and Consociational Electoral Engineering in Bosnia and Herzegovina”, p.336-337.

ethnic group is hardly ever monolithic, and thus there is always the risk of ‘flanking’ – the ruling elites can be labeled ‘appeasers’ and a ‘sell-outs’ by the competing intra-group elites for entering into agreements with the opposing ethnic group, in an effort to win over the polarized ethnic vote⁴⁴. This leaves the elites – even with the assumption that they are willing to do so in the first place – unable to freely engage in inter-group cooperation. This has been a tried and true tactic in Bosnia, the epitomic example of which is the fact that Milorad Dodik, the Prime Minister of Republika Srpska and the leader of Alliance of Independent Social Democrats (Savez Nezavisnih Socijaldemokrata – SNSD), a ‘moderate’ party strongly supported by the international community over its main competitor in RS, the radical Serb Democratic Party (SDS), is calling for Republika Srpska’s secession from Bosnia, while his Bosniac counterpart, the current member of the Presidency of Bosnia and Herzegovina, Haris Silajdzic, got elected on the platform of calling for the abolishment of the ‘genocidal creation’ – Republika Srpska. The latest elections, held in October of 2006, under the announced closure of OHR in June of 2007, brought back the kind of nationalistic rhetoric not seen since the very end of the war⁴⁵, and have to a great extent contributed to the PIC's decision to push back OHR's closure for the Summer of 2008.

Despite this seeming lack of compatibility for the situation in Bosnia, the Dayton type of consociationalism, at the time of its signing at the end of 1995, had only one other viable alternative – that of the factual dissolution of the country according to war-time ethnic divisions. Even though that option was rejected as a solution to end the fighting, the only other option nominally acceptable to all three parties, and yet failing to satisfy the main desires of any of them, was the Dayton solution: a highly decentralized, barely functional central government bereft of any enforcement powers and the creation of two highly autonomous ‘statelets’, Republika Srpska, and the Federation. The aim was to ensure constitutional protection of the vital interests of each of the ‘constituent’ people through minute

⁴⁴ Horowitz, 1985, p.573.

⁴⁵ OHR Press Release, November 8, 2006.

descriptions of a complex institutional system, but this brought with it probably the biggest, and arguably least effective bureaucracy in the world, relative to the population size. Some of the obvious drawbacks to such a governance system, especially in terms of its ability to provide Bosnia with a stable, self-sustainable future, will be delineated below.

Dayton Drawbacks

Role of the central government, according to Dayton, was limited to:

- * Foreign policy.
- * Foreign trade policy.
- * Customs policy.
- * Monetary policy.
- * Finances of the institutions and for the international obligations of Bosnia and Herzegovina.
- * Immigration, refugee, and asylum policy and regulation.
- * International and inter-Entity criminal law enforcement, including relations with Interpol.
- * Establishment and operation of common and international communications facilities.
- * Regulation of inter-Entity transportation.
- * Air traffic control.⁴⁶

All other competencies, including revenue-collection, defense, education, even the right to “establish special parallel relationships with neighboring states⁴⁷”, belonged to Entities, thus creating a central government weak enough to fit the confederal, not federal, description. The central government had no direct means of revenue collection, but depended on funding from the Entities. Over time some of the competencies of the entities have been transferred to the state level, gradually strengthening the central government. From the original of three state-level ministries (foreign affairs, foreign trade, and civil affairs), the number has slowly climbed to the present nine ministries. The creation of the State Border Service in 2000, and (nominal) unification of the separate armies into a unified military at the state level, as well as the 2003 creation of the state-level Indirect Taxation Authority (ITA) were the most important of those, however it is widely acknowledged that the central government is still far

⁴⁶ Constitution of Bosnia and Herzegovina, Article III.1.

⁴⁷ Constitution of Bosnia and Herzegovina, Article III.2.

from being able to meet the demands of legislative, economic and structural changes required for European integration⁴⁸.

As it stands, all state-level legislation is subject to a cumbersome process open to abuse by disruptive nationalist politicians, as all legislation, as well as the budget, must meet the approval of all three institutions of government (Presidency, Council of Ministers and the bicameral Parliament), oftentimes requiring prior approval from the Entities as well. Given the operational rules of the Council of Ministers, which can meet only with a quorum including at least one member of each constituent people, and can reach decisions only through approval by a majority of the ministers, further paralysis of the government is easy to achieve. This was most recently seen when Bosniac members of the Council failed to show up for a number of scheduled meetings, thus effectively blocking the operation of the Council⁴⁹.

Even when the governmental institutions work properly, they do not have the needed authority nor capacity to fully take on the role of central government, especially when faced with challenges of transition, and European integration. The highly critical Venice Commission report⁵⁰ on the constitutional structure of Bosnia, issued in March of 2005, has found that the Vital National Interest veto, the two-chamber parliamentary system that mainly replicates its work, and the collective presidency make effective government extremely difficult, if not impossible. Furthermore, the state government was found to be very weak against the powers of the Entities, and lacking the necessary capacity to lead the arduous process of European integration. Any country considering membership in the European Union is required to meet five basic conditions – it has to be (a) a stable democracy; (b) have a proven record of the rule of law and respect for and protection of minority and human rights; (c) has a functioning market economy that is capable of (d) coping with market forces and competitive pressures within the union; and (e) prove its ability to take on the obligations of membership, including

⁴⁸ ICG, 2007. Pp. 9-25.

⁴⁹ Glas Srpske, March 12, 2007.

⁵⁰ Venice Commission, March, 2005.

economic and monetary union⁵¹. Part of that ability is the adoption of the *acquis communautaire*, consisting of over 80,000 pages of EU law, covering subjects from taxation, judiciary, to environmental rights. The central government of Bosnia and Herzegovina, in the assessment of the Venice Commission, “is not able to effectively ensure compliance with the commitments of the country with respect to the Council of Europe and the international community in general,” and finds that it is “unthinkable that BiH can make real progress with the present constitutional arrangements.”⁵²

Finally, even if the political will to transfer sufficient competencies from the entity to the state level was found, and the disruption of central bodies was kept to the minimum by politicians, thus ensuring progress in implementation of reforms, the Dayton system of governance is simply not financially sustainable. With the state structure that includes fourteen governments, and four separate levels of administration (municipal, cantonal, entity and state level), employing over 760 legislators⁵³ and around 200 ministers⁵⁴ (as well as their deputies, secretaries, and chauffeurs), it is not surprising that over 60% of Bosnia's annual GDP comes from the 'services' sector⁵⁵. The proof that the government employees charge their services at a high rate is the fact that 70% of the public budget of Bosnia is spent on the vast bureaucratic machinery⁵⁶. The need to implement a centralized revenue and taxation system was not only a necessary precondition for EU accession, but also a much-needed short-term solution for the long-term unsustainable costs of running a barely functioning government.

Thus, in short, the highly structured Dayton 'blueprints' for the institutional set-up of the governance system in Bosnia create a number of obstacles for the further development and self-sustainability of the country. The central government as created by Dayton was too weak to truly

⁵¹ For full information, see Commission's website at www.ec.europa.eu/enlargement/enlargement_process/accession_process/index_en.htm

⁵² Venice Commission, 2005. Pp.8.

⁵³ European Commission Progress Report on Bosnia and Herzegovina, 2006. Pp. 6.

⁵⁴ Roland Kostic, 2002. Pp. 9.

⁵⁵ OECD Country Sheet for Bosnia and Herzegovina, 2006.

⁵⁶ OHR Press Release, December 15, 2005.

govern the country – instead, the highly autonomous Entities, often working at cross-purposes and rarely coordinating their economic or social policies, held most of the power, including revenue collection. The decision-making process on the central level is open to easy abuse and paralysis by obstructionist politicians, due to the cascading levels of approval, and veto powers of the Entities. Finally, even if obstruction was halted, and cooperation among Bosnia's three groups was assured, the sheer cost of operating the fourteen-government, four-layer system of governance is crippling for a country with unemployment rate of 45%, and the lowest GDP per capita in the region, after Albania⁵⁷.

OFFICE OF THE HIGH REPRESENTATIVE

There has been extensive academic work done on analysis of international administrations in general, focusing on their legitimacy, authority, practices, goals and/or organization, and on the work and presence of the international community in post-Dayton Bosnia-Herzegovina in particular. Depending on the author, the final judgment of the international administration in Bosnia, that of the Office of the High representative, runs the gamut from scathing (an example of new-age colonialism, actively undermining democratization⁵⁸), to those who have called for a stronger, more decisively interventionist role for the High Representative⁵⁹. The majority of reports, however, fit into an ambivalent middle ground – though certain actions of OHR may stand in direct opposition of democratic principles the Office is tasked with protecting, and certain side-effects of such actions will have a long-lasting negative impact on democratization, much of the efforts have been necessary, and, overall, the total sum of good vs. bad may end up in a positive column⁶⁰. One of the major themes in most reports is the tug of war between the international administration's exercise of political and

⁵⁷ OECD Country Fact Sheet, 2005. Pp. 15-16.

⁵⁸ Chandler, 2000. Knaus and Martin, 2003.

⁵⁹ International Crisis Group, 1996. Broden & Server, 2000.

⁶⁰ Bose, 2002. Bieber, 2005. McMahon, 2002. Knaus & Cox, 2000.

executive power over the administered territory, and its ultimate goal of instilling lasting democratic practices in the territory. As Dominik Zaum notes, the international administration's “exercise of political authority over post-conflict territories seems to be at odds with contemporary conceptions of legitimate government.”⁶¹

Duties of the Office of the High Representative were delineated in the Dayton agreement, and OHR was tasked with the “implementation of the civilian aspects of the peace settlement”. Unfortunately, in what will be deemed as showing the lack of actual will to implement the civilian aspects of Dayton, OHR's powers, as listed in Annex X of Dayton, were limited to “monitoring implementation”, “maintaining close contact” with all parties, “coordinating activities” of various civil agencies in Bosnia, and “reporting” on progress⁶² - thus, providing it with no power to impose any decisions, and no command over NATO or UN peacekeeping forces stationed in Bosnia. Given the weak-toothed mandate given to the High Representative, and the post-war polarization of the country still very much in the grips of the nationalist politicians that caused the war, logic dictated that the implementation of Dayton, based on voluntary compliance by all Bosnian parties, would be weak to non-existent. Indeed, during the initial years following the signing of the Dayton accords, there was little commitment on the side of Bosnian Serbs and Croats to implement the provisions of the agreement: leaders of both communities kept their eye on ensuring the secession of their war-achieved ethnically homogeneous areas and eventual joining to their titular motherlands, Serbia and Croatia. In short, the situation in Bosnia two years after the signing of the Dayton agreement, was not stabilizing: “Paramilitary groups terrorized parts of the country. Wartime leaders hung on, doing their best to frustrate the establishment of the political institutions created under the new constitution; refugees and displaced persons found their return home deliberately blocked; the weak and over matched OHR

⁶¹ Zaum, 2006.

⁶² Constitution of Bosnia and Herzegovina, Article X.

could do little to help.⁶³”

It was this kind of environment that, in 1997, prompted the Peace Implementation Council (PIC), the overseeing body for the Office of the High Representative, to give to the High Representative, under generous reading of Annex X, Article 5⁶⁴ of Dayton, the mandate to be able to draft and impose laws, remove obstructionist politicians, shut down hate-mongering media outlets, and so forth. In words of Paddy Ashdown, the fourth man to hold the position of the High Representative, the PIC and OHR were “not prepared to accept that hard-line officials could sabotage the provisions of the Dayton Agreement with impunity, or to cripple various governments and parliamentary assemblies, or hobble the legislative process, rendering it incapable of passing the legislation necessary to cement democracy and re-start the economy⁶⁵.” Its new mandate, popularly called the Bonn powers, effectively transformed OHR into the most powerful legislative and executive body in Bosnia.

There have been five different High Representatives since the signing of the Dayton agreement in 1995: Carl Bildt (1996-1997), Carlos Westendorp (1997-1999), Wolfgang Petritsch (1999-2002), Paddy Ashdown (2002-2006), and the current High Representative, Christian Schwartz-Schilling is set to be replaced in July by Miroslav Lajcak, presumably the person to oversee the closing of OHR in July of 2008. Since the Bonn powers were granted to the High Representative in 1997, there has been an almost exponential increase in the number of laws and decisions handed down by the High Representative – over 100 laws were passed, and several hundred decisions handed down⁶⁶.

Four general phases of the use of the Bonn powers can be distinguished. In the first one, at the very beginning, the focus was on establishing “the core elements of state identity” such as a citizenship law, a national flag and anthem, a currency, and uniform license plates to facilitate freedom of movement. With HR Petritsch, the focus shifted on creation of key state-level institutions (ex. State-

⁶³ Knaus and Martin, pp. 63.

⁶⁴ Article 5 reads: “The High Representative is the final authority in theater regarding interpretation of this Agreement on the civilian implementation of the peace settlement.”

⁶⁵ Venice Commission, 2004. Pp.21.

⁶⁶ List of all decisions can be found at www.ohr.int

Border Service), and establishment of structural basis for a functioning economy (consolidation and reform in the areas of taxation, privatization, and payment systems.) Ashdown earned the title of a 'European Raj' due to his extensive use of the Bonn powers to remove obstructionist and corrupt officials, in an effort to ensure application of previously enacted laws⁶⁷. Where Ashdown was accused of excessively using OHR's "unchecked powers", Schwartz-Schilling has been faulted for his lack of quick and decisive action, and decision not to use the Bonn powers unless absolutely necessary⁶⁸. This has been a logical approach, given that Schwartz-Schilling's mandate was to prepare OHR for a gradual phase-out and closure, however – given the deteriorating situation in the region – a worry has been expressed that focus on internal OHR issues “will keep the OHR’s staff busy for the coming twelve months while Bosnia may well be slipping into a serious crisis⁶⁹.”

This kind of sweeping use of legislative and executive powers by a civilian administrator with no popular mandate, and no accountability to the people of Bosnia, has not been without criticism. Though there was some initial support for the stronger interventionist policies of the OHR in Bosnia, most notably from the International Crisis Group⁷⁰, a policy advocacy group based in Brussels, by the late nineties there have been calls to curb the use of OHR powers, as, it was argued, they limit and hobble the development of democracy in Bosnia and actually strengthen nationalistic parties and leaders.

Whereas ICG's reports called for a decisive, top-down approach to state-building in Bosnia by the international community, a number of other assessments point out the negative direct or side-effects of international involvement or the outright failures of its policies. European Stability Initiative, an influential policy institute specializing in SEE issues, has argued that international community's

⁶⁷ T.K. Vogel, 2006. Pp.7.

⁶⁸ Numanovic, “Glavni poraz međunarodne zajednice je neuspjeh ustavnih promjena”, interview with Andrzej Tyszkiewicz, Polish Ambassador to Bosnia. Avaz on-line, May 19, 2007.

⁶⁹ CEIS, July 2006.

⁷⁰ ICG, 1996, 1999.

involvement “into the intricacies of decision-making at all levels of the Bosnian political system⁷¹” has fundamentally altered the dynamics of the political process in the country, and not in a positive way. In an open letter to the then-High Representative, Paddy Ashdown, they warn that the policies of the Office of the High Representative continue and preserve the worst tendencies of the pre-war communist culture – that of “the 'strong hand' that acts as a *deus ex machina* outside the political process⁷².”

This sentiment was expressed even more strongly by Gerald Knaus and Felix Martin, two analysts with ESI, who tacked a title of a 'European Raj' to Paddy Ashdown in a critical paper, calling for an immediate curbing of his use of the Bonn powers. They argued that “along a path punctuated by crises, the OHR's autocratic powers have grown in scope and severity from nothing at all, through powers to impose sanctions and the interim laws designed to support the Dayton process, to absolute powers over an open ended spectrum of issues. ... Far from planting the seed of democratic politics in Bosnia's post communist political culture, this transformation implicitly teaches that technocratic rule at arm's length from the people is perfectly good governance after all⁷³.” This kind of assessment of the effect of international administration on the development of a sustainable, democratic state, institutions, and political processes is not limited to ESI. Indeed, the current HR Schwarz-Schilling, is a long-time ESI supporter, with close ties to two of its three founding board members, and strongly shares this opinion⁷⁴.

Three main arguments emerge from the analysis of OHR's influence on Bosnia's political development, sustainability and democratization – the top-down imposition of common institutions perpetuates the image of Bosnia as an artificial state, and undermines their effectiveness, and trust of the populace; has a direct negative impact on democratization, as it uses unquestionable decree powers

⁷¹ ESI, 1999.

⁷² ESI, 2003.

⁷³ Knaus and Martin, pp.69 -70.

⁷⁴ ESI website, 2006. “Christian Schwarz-Schilling, the new High Representative.”

against democratically elected officials, perpetuating communist-era practices; short-circuits the decision-making process in Bosnia, making the local politicians both used to, and dependent on outside intervention, and unwilling or unable to engage in the political bargaining game that would require them to both make difficult decisions, and be accountable for them.

Robert Hayden, a proponent of ethnically-homogeneous states with uncomplicated constitutions, has argued that both the Dayton, and the Federation constitutions (as well as the geopolitical entities they enshrine) are, in effect, Frankensteinian creations more suited for the dissecting table than active implementation. In his view, the Office of the High Representative has had to actively impose Bosnia upon the Bosnians, in order to overcome the innate contradiction of the country – an existence of a sovereign, unitary state without a functioning central government. Thus, in Hayden's view, “[t]he more that the High Representative ignores the need for the people of Bosnia themselves to consent to be governed by a Bosnian state, the less legitimate that state is likely to be to those whose consent was conditioned on its being illusory.⁷⁵” ESI's 1999 report mirrors that assessment, without sharing Hayden's belief in the overall artificiality of the Bosnian state. They find fault in the OHR's approach to the root cause of problems, not the general fact of its involvement; instead of focusing on dismantling post-war power structures, OHR focused its efforts on building and propping up joint state-level institutions which had no support from nationalistic Serb and Croat politicians in power at that time⁷⁶.

This directly translates into the second argument, which argues that the kind of top-down imposition of laws and decrees by OHR, though initially controversial, had become routine by the early 2000s, attracting little negative response from Bosnian public and political elites, if not being actively lobbied for by them. This would indicate that there is an obvious lack of democratic accountability and political autonomy in the country, which opens international administrations to the charges of

⁷⁵ Hayden, 1999. Pp.138-39.

⁷⁶ ESI, 1999. Pp. 17-18.

'neocolonialism'⁷⁷, but – more importantly – perpetuates the kind of authoritarian decision-making style popular with the pre-war communist regime. The ten-year 'Bonn Powers' rule of OHR has had the effect of “replacing the arbitrariness of previous regimes with that of the international community⁷⁸,” maintaining the “authoritarian temptation” legacy of the past regime. In words of ESI, the authoritarian temptation is “the belief that policy (mainly understood as legislation) can best be formulated outside the political process, and imposed on society without the participation of stakeholders⁷⁹.” This caused, in words of Wolfgang Petritsch, a state of passivity in Bosnia and Herzegovina – “a passivity that is not typical Bosnian, as some people claim, but typical of post-authoritarian societies⁸⁰”. OHR's maintenance of this tendency to look to outsiders to solve Bosnia's problems, rather than finding home-grown solutions, has an impact on the expectations and behavior both of the public, and of the local politicians. If the electorate, or the civil society at large, feels that they have limited means to influence policy-making in the state, there will be no incentive for them to remain engaged and keep trying. On the other hand, the local political elites, instead of being provided with initiatives and leadership to move away from the technocratic type of socialist leadership of the pre-war period, are learning from OHR what kind of leadership strategy they will be able to employ in Bosnia upon the departure of international administrators⁸¹.

In the short-run, however, the process of political self-sustainability is further negatively impacted by OHR's policies. This type of intrusive, nearly paternalistic international presence has stunted the development of democratic processes, and contributed to a situation in which Bosnian elites refused to take responsibility for building functioning institutions. The process of building and strengthening state-level institutions would have demanded the kind of political compromise and difficult decisions that would have proven unpopular with the constituencies of local politicians,

⁷⁷ Zaum, 2003. Pp.116. Chandler, 1999.

⁷⁸ Knaus and Cox, 2000. Pp.11.

⁷⁹ ESI, 2004. Pp 49.

⁸⁰ Solioz, 2003. Pp360.

⁸¹ ESI, 2004. Pp. 3.

especially in the Croat and Serb areas. Given the fact that OHR was able, and willing to step in and impose needed legislation and create state-level institutions, the local politicians were able to avoid any kind of responsibility for the development of the Bosnian state – the much-lauded sense of 'ownership', both of the process itself, and of the fate of the country⁸².

This, in turn, caused the development of widespread dependency syndrome in the country, both in the economic and political arena. Council of Europe (CoE), found the situation unsustainable in the long run, and the Parliamentary Assembly of that body adopted a resolution in 2004 that considered it “irreconcilable with democratic principles that the OHR should be able to take enforceable decisions without being accountable for them or obliged to justify their validity and without there being a legal remedy⁸³.” The Venice Commission, the legal arm of CoE, issued in March of 2005 an opinion on the Constitution of Bosnia and Herzegovina, and on the powers of the High Representative in which it acknowledged that, from a political point of view, numerous actions by the OHR have been beneficial for Bosnia and Herzegovina. However, the Commission went on to say that:

“such an arrangement is fundamentally incompatible with the democratic character of the state and the sovereignty of BiH. The longer it stays in place the more questionable it becomes. There is a strong risk of perverse effects: local politicians have no incentive to accept painful but necessary political compromises since they know that, if no agreement is reached, in the end the High Representative can impose the legislation. So why take responsibility and not leave it to the High Representative? A dependency culture incompatible with the future development of BiH risks being created.⁸⁴”

Here, again, we see the warning that OHR's practices, instead of helping democratize the country, and instill a sense of “ownership”, have had the effect of creating or, more accurately, preserving a dependency culture remaining from the pre-war, communist mind-set of autocratic rule,. Thus, it can be said that the kind of 'short-circuiting' of the decision-making process by OHR, where outside 'experts' can step in to draft and impose important legislation, has not only held Bosnia back from the full transition from the pre-war socialist system of governance to a democracy, but has added the

⁸² Fischer, 2006. Pp446.

⁸³ Council of Europe, Resolution 1384. June 23, 2004. Available at www.coe.int.

⁸⁴ Venice Commission, March 2005. Pp.22.

burden of another transition, that from dependency on the international community, to self-sustainability⁸⁵.

POLITICAL ELITE IN BOSNIA

(And the Socialist Governance Legacy)

As seen in the previous section, the role of the international administration in Bosnia had a strong effect on the democratization process (or lack thereof) in the country. The need for much of the international intervention, nor the full effects of it can be analyzed in a vacuum. A strong interventionist attitude by the international actors, as mentioned, was needed as a response to equally strong obstructionist policies of hard-line nationalist leaders. The current culture of dependency of the national elites on the 'strong hand' of the OHR, and the lack of their accountability to their electorate cannot be in blamed in full on the strong interventionist policies of the international administrators – if there had been a desire of the political elites to take responsibility for the future of the country, OHR would not have had to play such a strong role on Bosnia's political scene. The question of what came first, the chicken or the egg of the dependency syndrome in Bosnia – are Bosnia's political elites unable and unwilling to work towards a compromise for the sake of the common future due to role OHR played in the decision-making process, or is the HR's willingness to cut short the messy and prolonged process of 'democracy' in Bosnia due to the current unwillingness of its players to take responsibility is a moot point; both factors are prominently present in Bosnia today, and play an important role in its future.

Dayton agreement, and the constitutional set-up it brought forward, maintained the reality of Bosnia as a unified state, even if only in the most provisional way. The Office of the High Representative, and other major international players on the scene, expanded the meager institutional

⁸⁵ Zeljko Papic, as quoted in Solioz, 2003. Pp. 359.

provisions of Dayton by creating and strengthening common institutions, and strengthening the role of the central government. Despite the strengthened framework of a central government within the unitary borders of Bosnia and Herzegovina, it is the local politicians who fill out its outlines, and staff its offices. The machinery may be tailored to look and function a certain way, but if the technicians in charge of operating it are opposed to the end product to be created by its smooth running, logjam is easily created.

There are a few basic and instrumental attributes of the political actors staffing Bosnia's political machine: war-time nationalist parties still command a great deal of power in the system, and have goals that are oftentimes diametrically opposed to one another; nationalist rhetoric, though not necessarily based in true ethnic hatred, still wins elections; the *nomenklatura* mindset of the socialist era, where the dominant party controls allocation of privileges, important positions and resources, has been perpetuated and fused with the new “kleptocracy” of the war-time racketeers into a system where political and economic goals of the ruling elites take precedence over democratization and development. Furthermore, Bosnia's politicians still practice the socialist-era way of governance that favors decision-making based on “expert” opinions as opposed to the democratic process of negotiation and compromise, a process that in turn fosters the “passivity of public institutions.”⁸⁶

Twelve years after the end of fighting in Bosnia, there still exists only marginal support for parties which run on a multiethnic, non-nationalist platform. The most recent elections in Bosnia in October of 2006 were marked by escalating nationalistic rhetoric and electoral wins by the leaders of the two parties seen as 'moderate' options to their nationalistic counterparts – Party for Bosnia and Herzegovina (SBiH) of the current Bosniac member of the Presidency, Haris Silajdzic, and the Alliance of Independent Social Democrats (SNSD) of the Prime Minister of Republika Srpska, Milorad Dodik. Where SBiH was seen as a more moderate and less ethnically-oriented than the main Bosniac party in Bosnia, the SDA, Silajdzic won the Bosniac vote for the Presidency by calling for the abolition

⁸⁶ ESI, 2004. Pg.3.

of the “genocidal creation”, Republika Srpska. Dodik for his part, strongly supported by the international community during his first run as a Prime Minister of RS in 1997-1999 as a preferred moderate over the SDS, achieved a landslide victory for SNSD in the elections by calling for an independence referendum in Republika Srpska. As reported by ICG, just two of the 36 parties running in the elections – the SDP (Socialdemocratic Party) and Radom za Boljitak (Working for Improvement) – had civically oriented platforms, while 26 had no platforms at all⁸⁷. Where the SDP Presidency candidate, Zeljko Komsic, won over the candidates of the nationalist Croat parties HDZ-BiH and HDZ-1990⁸⁸ (mainly through support of Bosniac voters), the party itself remained in the opposition in the state and Federation Parliament⁸⁹. In short, though the most recent elections shifted the balance of power between political parties in BiH, they have not broken the pattern of ethnically divisive politics, and, given the recent developments, may have even reinforced it⁹⁰. When compared to the last elections, where the war-time nationalist parties, SDA, SDS and HDZ swept into power after a brief 2001-2002 period, the win of the nominally more moderate parties – SBiH and SNSD – is not very encouraging. The election-time inflammatory rhetoric, and nationalist agenda of the 'moderate' parties, as well as the break-down in the reform process caused by their continued obstructionist policies, does not compare well with the previous 2002-2006 nationalist government. Compare Ashdown's assessment of the previous government:

“[the] self-styled ‘nationalist parties’ who won the Bosnia and Herzegovina elections in October 2002 have presided over the strongest period of change and reform in Bosnia and Herzegovina’s post Dayton history—and some, at least, appear now to want to internally reform themselves away from the old style

⁸⁷ ICG, 2007. Pg.19.

⁸⁸ HDZ-1990 was created by a group of HDZ-BiH politicians that felt that the “original goals” of HDZ BiH were not being met by the current leadership. They split from the main party in 2006, and HDZ 1990 was seen as courting the votes of the more hard line Croat supporters. The Economist Intelligence Unit Country Report for Bosnia-Herzegovina, July 2006. Pp.17.

⁸⁹ Full election results available from Central Election Commission of Bosnia-Herzegovina.

⁹⁰ Silajdzic and Dodik, seen as key players needed to further key reforms needed as a precondition of Bosnia's signing of the SAA, have been engaged in a war of words that continued past the elections. Most recently, they failed to reach any kind of an agreement on police and constitutional reforms at a 3-day meeting in Washington organized by the State Department and the American Ambassador to Bosnia. “Bosnia talks end in disarray”, Financial Times Online, May 25, 2007.

nationalism of the war years and towards more conventional center right European politics.⁹¹”

with that of the current HR, Schwartz-Schilling, commenting on the continued nationalist rhetoric six months after the October elections:

“After six long months in which we have seen a great deal of acrimony and little constructive dialogue, a dramatic change in the tone of political debate in Bosnia and Herzegovina is overdue. Even after the elections, many parties reduced their public pronouncements to the level of slogans – easy on the ear, pleasing to some constituents, but far short of a serious response to the complex challenges facing this country and all its citizens.⁹²”

The current contextual factors play a strong role in the deterioration of political cooperation and intensification of nationalist rhetoric. The waves of instability spreading from the future status of Kosovo have, after Serbia itself, strongest effects in Bosnia. Serbian Premier Kostunica has been linking future of RS with the now inevitable independence of Kosovo, which in turn has encouraged Dodik's statements on referendum⁹³. The International Court of Justice's (ICJ) March 2007 verdict in the lawsuit that Bosnia-Herzegovina had brought against Serbia has caused further instability. The ICJ ruling that genocide was committed in Srebrenica by Bosnian Serb forces has been used by Silajdzic to strengthen his calls for the abolishment of RS. In the face of that decision, SBiH-appointed Foreign Minister, Sven Alkalaj, unilaterally proclaimed dual-citizenship agreement between Bosnia and Serbia⁹⁴ invalid, causing an uproar by the Serb politicians, and the Serb member of Bosnia's Presidency, SNSD-appointed Nebojsa Radmanovic, vetoed the decision of the Bosniac and Croat members, Silajdzic and Komsic, to issue an official declaration demanding that Serbia comply with the decision of ICJ, and arrest war crimes suspects in its territory⁹⁵. The announced closure of OHR, though moved for July of 2008, combined with the non-interventionist policy of the current HR, has

⁹¹ November 2005 speech by Paddy Ashdown on the occasion of the tenth anniversary of the Dayton accord. OHR, November 18, 2005.

⁹² OHR Press Release, April 06, 2007.

⁹³ ICG, 2007. Pp. i.

⁹⁴ B92 News Website, March 6, 2007. “Dual Citizenship Still Stands.”

⁹⁵ Katana, April 2007. After Radmanovic issued a veto on the decision, Parliament of Republika Srpska confirmed that such a Presidential declaration represented a violation of the vital interests of that entity, upholding Radmanovic's veto.

encouraged obstructionist actions of RS politicians, especially Milorad Dodik, who seem to be content to block further reforms and integration while waiting for the departure of OHR⁹⁶.

Though these contextual factors are conducive to the polarization of the political situation in the country, the current deterioration of political dialogue and lack progress would not have had to happen if the politicians found benefit in cooperation and compromise. A major obstacle to cooperation and compromise is that the political elites, if not Bosnia's population at large, have diametrically opposing goals. Whereas Serb leadership still sees unification of RS with Serbia as the ultimate final goal, with the independence of RS as an interim step⁹⁷, the Bosniac leadership seeks the eventual abolishment of the Entities, and full reintegration and centralization of the country. Though Croat separatist efforts have lessened since the death of Croatia's war-time President, Tudjman, Croat politicians feel that further centralization of Bosnia would be “detrimental to the political position of Bosnia's Croat citizens⁹⁸,” preferring to keep most of the power on the (ethnically homogenized) cantonal level.

Decentralization of power to the ethnically homogeneous entity/canton levels helps preserve political control in the hands of political elites willing and able to use nationalist rhetoric as a divisive tool. As has been noted, nationalist parties in Bosnia inherited communist-era tools of social and economic control, only amplified by their war-time “monopoly on violence and their control of informal economic activity.⁹⁹” ESI, in its 1999 assessment of the power-structures in Bosnia found that the nationalist leaders of the three ethnic groups, while clearly oppositional in certain areas, all depend on the same basic conditions for maintaining their power: “ethnic separation; public fear and insecurity; a lack of democratic accountability; breakdown in the rule of law; and a lack of institutions capable of controlling illegal economic activity.¹⁰⁰” Given that, it becomes clear why the goals of the Dayton agreement (facilitation of minority return, creation of independent, multiethnic institutions such

⁹⁶ CEIS, 2006. In response to Dodik's referendum threats, OHR responded with the message that a referendum was not an option for as long as OHR remains in Bosnia. Pp. 4.

⁹⁷ Lyon, 2006. Pp.54.

⁹⁸ Economist Intelligence Unit, July 2006. Pp.14.

⁹⁹ ESI, 1999. Pp. 2.

¹⁰⁰ Ibid, pp. 3.

as the Central Bank, the Public Service System, or carrying out basic economic reforms, and the reintegration of the economic space), were strongly resisted by Croat and Serb nationalist parties. Such integrative reforms “were resisted because they were seen as threats to party’s interests, and consequently, explained as threats to existence of an entire ethnic group.¹⁰¹” Though supportive of greater centralization pursued by the international community, the Bosniac nationalist parties also relied on the conditions of continued corruption, public fear and insecurity, and ethnic separation as a means of holding on to their power. In truth, nationalist elites in Bosnia “had no incentive to allow control over their affairs to shift to new institutions, which they could not be sure of controlling.¹⁰²”

The situation is further complicated by the autocratic legacy left over from the pre-war, communist period, and the strong web of war-time criminal networks grown rich and powerful on weapons smuggling, human and drug trafficking, and other illegal activities. The socialist-era *nomenklatura* system of governance, where the “dominant party through its various bodies and committees controls all significant appointments, promotions, allocation of privileges and dismissals¹⁰³,” including the legislative, judiciary as well as economic positions, was preserved by the nationalist parties. This was a continuation of the political culture left over after fifty years of Communist Party rule – the party has direct control over military, state, administrative and judicial institutions. With the three nationalist parties, HDZ, SDA and SDS, sweeping first democratic elections in the post-war period, and thus gaining a level of democratic legitimacy, this kind of governance was preserved despite the Dayton-created central government institutions. This was translated into three separate and parallel power structures in post-war Bosnia. Especially visible in the Federation, in Croat-majority cantons HDZ established and controlled separate education and health care systems, as well as a separate military and intelligence forces, with only symbolic participation in

¹⁰¹ Selo-Sabic, 2005. Pp. 37-38.

¹⁰² Knaus and Cox, 2000. Pp.10.

¹⁰³ ESI, 1999. Pp. 4.

Federation and state government¹⁰⁴.

Though the Herceg-Bosna parallel structures ran and financed by HDZ have generally been dismantled following lack of continued funding from Croatia starting in 2000, and strong international pressure, and central government and institutions have been strengthened in the past five years, parties in power in Bosnia still have strong influence in terms of allocation of important legislative and administrative positions. As Martin Cox notes: “In many smaller towns across Bosnia, a single enterprise provides the bulk of employment, and control of the enterprises is a potent source of political power. ... Complex systems of bureaucratic licensing of private enterprise ensure that political contacts are needed for commercial success, which fosters official corruption.¹⁰⁵” This has perpetuated public apathy and lack of belief in the democratic process, as the people are “well aware that real political decisions were not taken in the parliaments,¹⁰⁶” undermining the development of a responsive civil society.

The autocratic legacy of the socialist-era one-party rule extends beyond the control that the ruling parties have over the allocation of jobs in the public and private sectors, it influences the entire approach to governance. In socialist Bosnia, there was no “genuinely open” process during which different interest groups could hash out differences and come to a mutually accepted compromise on any number of important social and economic issues. Instead, a “rule making elite” was at the helm of public administrations, relying on the input of the “expert¹⁰⁷” - to shape their policies, a process that in turn fosters the “passivity of public institutions.¹⁰⁸” The passivity of public institutions, and reliance of the 'rule making elite' on the opinions of experts who are outside of the democratic decision-making process is clearly present in today's Bosnia, a country whose entire reform process is engineered, powered, directed and driven by a large number of international organizations and foreign

¹⁰⁴ Bieber, 2005. Pp65-66.

¹⁰⁵ Cox, 2001. Pp. 8.

¹⁰⁶ ESI, 1999. Pp. 4.

¹⁰⁷ ESI, 2004. “The technician who was thought to be best placed to determine the public interest,” pp. 3.

¹⁰⁸ ESI, 2004.

governments.

Another legacy influencing development of democratic and transparent institutions is the war-time symbiosis of political elite with organized crime and illegal economic activity. During the war, nationalist parties and the armed forces they controlled ensured funds for their political and military goals by controlling the movement and sales of food, fuel, alcohol, etc. In the after-war period, when free movement of goods made these articles widely available, new forms of criminal activity took over, among them drug trade, and human trafficking¹⁰⁹. In the after-war period, demobilized soldiers and paramilitary groups got absorbed by, or transformed into organized criminal networks, while maintaining close links with political decision-makers¹¹⁰. Organized protection of indicted war criminals is also an example of continued cooperation of organized crime with nationalist parties. Per the CARPO Situation Report for 2006 on Organised and Economic Crime in South-eastern Europe, “[F]inancing runaway indicted war criminals, particularly Ratko Mladic and Radovan Karadzic, appears to be well organised and connected with a number of institutions such as banks, governing and other public institutions, and political parties in Republika Srpska.¹¹¹” As Bose unflatteringly notes:

“‘Nationalists’ in the post-war Bosnian context are often wartime racketeer networks, grown rich on an abnormal political and economic situation, who manipulate the fears of the impoverished people of their respective groups in an effort to preserve their own dominance, and profit-making. Their apparent espousal of the collective identity and common interests of their national group is often simply a superficial ideological camouflage for their racketeering activities.¹¹²”

This kind of criminal symbiosis of politicians and organized crime has been blatantly confirmed a number of times by the continued failure of the Parliament to pass a law that would have made

¹⁰⁹ Reliable data is difficult to obtain due to the fragmentation of Bosnia's criminal justice system – there are four jurisdictions; one on the State, two on the Entity levels, and one for District of Brcko – and lack of coordination and information sharing between their law-enforcement agencies. According to the CARPO Situation Report for 2006 on Organised and Economic Crime in South-eastern Europe, Bosnia is designated as a 'redistribution centre' for drugs trafficking, and as having a 'clandestine and sophisticated' human trafficking and sex exploitation business, with strong ties with traffickers from Serbia, Romania and Moldova. CARPO Situation Report, September 2006. Pp. 82-84.

¹¹⁰ ESI, 1999. Pp. 6.

¹¹¹ CARPO Situation Report, pp. 81.

¹¹² Bose, 2002. Pp. 6-7.

confiscation of illegally acquired property easier and more efficient¹¹³. According to the State Investigation and Protection Agency (SIPA) activity report for 2006, its department for combating economic crime made 23 reports against 40 individuals on the suspicion that they laundered more than 25 million Euros, noting the lack of efficient legal process for the confiscation of illegally acquired property¹¹⁴.

It would be logical to think that this kind of blatant corruption and criminality would lead to a change in power during the next elections, as the voters express their displeasure. Over 70% of people in Bosnia find both the governing and opposition parties completely untrustworthy¹¹⁵, exposing a widespread and prevalent contempt for the business of politics. However, instead of energizing organization of interest groups and a strong civic call for accountability of politicians, lack of respect for politicians, and expectations of their constructive performance, has translated into voter apathy and low level of democratic involvement by civil society, further cementing the position of nationalist parties.

Thus, the key characteristics of the Bosnian governance structures, and the effect they have had on the development of a self-sustainable democracy in Bosnia were summarized thusly by Christophe Solioz: “The old nomenklatura and the new kleptocracy worked hand in glove with organized crime and the remnants of the security services against any transition to democracy and the market economy¹¹⁶.” The socialist-era nomenklatura system where 'the party' had the absolute grip on the main political, social and economic institutions was simply fragmented among the three ethnic groups with the onset of war, not replaced by democratic governance, and further augmented by the support and interaction with the vast organized criminal networks that sprung up during the war. This type of governance has proven to be 'remarkably resilient' in the post-war period, benefiting in the large part by

¹¹³ Avdic, July 2004.

¹¹⁴ Kalamujic, February 2007.

¹¹⁵ International Commission on the Balkans, 2005. A 2005 questionnaire by the International Commission on the Balkans found that 77% of people asked to evaluate the current government marked their performance as 'Bad', and 71% gave the same mark to the opposition parties. Pp.40-41.

¹¹⁶ Solioz, 2001. Pp. 24-26.

voter apathy and general passivity of the civil society in Bosnia and Herzegovina.

CASE STUDY – VAT LAW IN BiH

Introduction

Law on Value Added Tax (VAT) in Bosnia was hailed as one of the most important reforms achieved by the Bosnian government, and as instrumental to set Bosnia on a path of European integration. The Office of the High Representative has repeatedly stressed the establishment of a unified indirect taxation system as one of the “essential preconditions for [EU] membership¹¹⁷,” and the passage of the Law on VAT was seen as a success, not only for managing to streamline a Bosnia's fragmented taxation system, but also because the process surrounding it was seen as being based on reforms and facts, not on separate ethnic interests¹¹⁸.

This section will seek to answer why is the VAT Law considered such an important step toward the country's advancement, and to what extent it was either advanced or hindered by the three factors discussed previously. Was this truly a local accomplishment, an example of much-needed 'ownership', or did the actors of the international community provide the drive for much of the successes? To what extent did the complex institutional structure of the decision-making bodies, and the decision-making process itself hinder the passage of the law, or was Bose correct in his assessment that, despite its complexity and cumbersome procedures, the Dayton consociationalism in Bosnia could function if Bosnia's politicians did not actively seek to paralyze the system? Finally, what does this particular episode tell us about the political elites in Bosnia? Can we detect a significant amount of 'ownership' of the processes, an advancement in the art of democratic policy-making – including the much needed need to compromise, and stand accountable for one's political decisions – or is this another example of

¹¹⁷ OHR Press Release, February 12, 2003.

¹¹⁸ FAST Update, Quarterly Risk Assessment, December 2004. Pp. 4.

the “passive government” syndrome, where the local politicians are beholden to everyone but their constituents? Is the decision made explained as inevitable due to interference by outside actors, subject to powerful criminal elements, or one based on careful analysis of the hard economic facts and figures?

The Basics: Value-Added Tax

The taxation system of a country is the life-blood of its government. Revenue collected from businesses and citizens is used to fund government expenses, and create development programs and policies – taxes pay for everything from better roads, schools and universities, social programs, to police and defense. It can also be used to stimulate, or cool the economy – tax breaks can make it easier for new businesses to be established, or first homes to be bought. In that grand scheme of things, there are two main streams of revenue for the government – one stemming from direct taxes (taxes on business and investment income of companies and individuals), and indirect taxes (taxes on imports and exports – customs fees, and taxes on consumption, which can be assessed in different manners – value added tax is used in the EU, while a sales tax is used in the US). In fiscal theory, lower direct taxes help stimulate the economy, as a greater post-tax income means more investment and growth of companies, and more spending by individual consumers, or, conversely, a hike in direct taxes can be used to equalize or increase the burden on the economically better-off portion of the population. On the other hand, indirect taxes, especially if levied in the VAT form, where the tax burden is transferred to the final customer, not the suppliers in the chain of supply, is used to spread the tax burden over the entire population of the country, even those with very low, or no income who otherwise would pay direct taxes.

In Bosnia, though the tax policy was administered at the Entity level, all three tax administrations (one each for the Federation, Republika Srpska, and District of Brcko) used retail tax as

a means of indirect taxation. Value-added tax, on the other hand, has been used as a means of consumption taxation in all of the countries of the European Union. The reason for this was the proven superiority of VAT over the retail tax system. VAT, as a form of consumption taxation, has been deemed superior to its alternative, the retail (sales) tax for two main reasons: it does not distort the production process, and it does not have a cascading effect. If a producer has to pay a sales tax on intermediate products needed to produce a good or create a service she is about to sell, there will be a distortion of a total cost of the product, as the tax of all the intermediate steps will be added in. This creates a cascading effect, as the tax is levied on both inputs and outputs of the same production process. This highly increases the overall tax burden of the producer than would be the case if the tax was levied only on final consumption. With VAT, however, a refund on the tax costs of all intermediate steps is available, thus keeping the final cost of the good transparent, and lifting the burden of added tax cost from the producer.

Lastly, even though only final consumption is taxed, due to the fact that everyone in the VAT chain is taxed along the way, the VAT system provides for much better tax collection, as anyone wanting a refund will have to report their activity. This way the VAT can be used to combat the gray economy and tax fraud.

Why VAT in Bosnia and Herzegovina?

There is a number of strong reasons for the implementation of a VAT system in Bosnia. The most obvious one is potentially the most important one – no country can start the accession process to the European Union, or even truly develop a fully beneficial trade relationship with its single market, without employing the VAT system. Candidate countries, and the countries in the region working toward the candidacy status, are required to harmonize their fiscal systems with the European

standards, and the EU's Sixth VAT Directive¹¹⁹ clearly delineates requirements to be met by candidate and member countries. Additionally, by the time the law was implemented in 2006, Bosnia was the last country in Europe, including all of the countries in the region, to implement it. Aside from the obvious and general benefits of the VAT system, some advantages of the system were specific to Bosnia, due to its singular institutional set-up.

From a purely economic perspective, the VAT system had a number of obvious advantages for Bosnia's economy. As mentioned, until late 2003 when the Indirect Taxation Agency law was passed, the indirect tax policy in Bosnia and Herzegovina was administered at the Entity level. This meant three separate tax administrations, three separate customs administrations and thus three separate sets of sales tax and excise tax laws. There were obvious negative structural and cost effects this had on development of companies wanting to do business across the whole area of Bosnia and Herzegovina – due to different direct and indirect taxes across the entities and District of Brcko, companies had to follow two to three different tax reporting procedures, and own separate bank accounts in entities in which they were doing business.

The International Monetary Fund identified additional drawbacks to the way tax administration was handled in Bosnia. Namely, due to the lack of coordination between the three tax administrations, the effects of different tax policies in an economic area with no internal borders caused significant tax competition. The Federation had a standard sales tax rate of 20 percent, and a reduced rate of 10 percent, while the sales tax on services was 10 percent. In Republika Srpska, however, the standard sales tax rate was 18 percent, and the reduced rate, as well as the sales tax on services, were set at 8 percent¹²⁰. The Brcko rates were similar to those in RS. Due to lower sales taxes on such basic goods as fuel, coffee, alcohol and cigarettes in RS, importers 'flocked' to that entity, causing annual revenue

¹¹⁹ For more information on European Union's VAT standards, consult European Commission's Taxation and Customs Union website at http://ec.europa.eu/taxation_customs/taxation/vat/index_en.htm.

¹²⁰ IMF, 2005. Pp. 75.

losses of some \$15 million annually to the Federation¹²¹. Furthermore, lack of coordination between the tax administration, especially in terms of verifying taxpayer returns, caused major revenue losses due to tax fraud¹²².

Value added tax system also has clear benefits in terms of improving Bosnia's overall trade balance and economic development. In 2004, Bosnia's trade balance deficit, the difference between its exports and imports, was close to one billion Euros¹²³, indicating that development and market share of domestic producers was strongly impacted by goods and services imported from abroad. Value-added tax is proven to have a double effect on the trade balance: it stimulates export of domestic goods, as exports are taxed at the zero-rate. This means that Bosnian exporters would receive a tax refund on the taxed costs of production of all exportable goods, including refund of taxes paid on electricity, raw materials, building materials used in production of the exported good. On the other hand, VAT discourages consumption of foreign goods, as VAT is charged on the total value of any imports – thus increasing their final cost in the country – whereas under the previous system the border sales tax was charged only on low-cost goods. The combination of higher exports and lower imports, aside from having a positive effect on Bosnia's trade deficit, would also stimulate growth of domestic production, bringing with it a lower number of unemployed. Bosnia's labor force is estimated at 1.1 million, out of a population of about 4 million people. Of that number, 45.5% are estimated to be unemployed – mostly due to the weak domestic production¹²⁴.

In addition to improving Bosnia's trade balance, it is anticipated that an integrated taxation system will also make Bosnia's economy a more attractive destination for foreign investors. The previous complex taxation system, unsynchronized regulation and strong gray economy all made Bosnia less appealing to foreign direct investment (FDI). As Paddy Ashdown noted: “When foreign

¹²¹ Alic, 2003.

¹²² IMF, 2005. Pp. 73.

¹²³ OECD, 2005. Pp. 14.

¹²⁴ Ibid., pp. 15.

investors look at BiH, they see two economic administrations, two bureaucracies, two sets of paperwork for everything. In fact, two economies too small and too complex to be worth investing in, so investors take their money to neighboring countries that have more normal and more simple systems. The result: jobs lost for BiH.¹²⁵”

Last, but not least, are the benefits of a VAT for the efforts to combat the gray economy, and avoid revenue losses due to tax fraud. According to IMF, estimated annual revenue loss due to tax fraud in Bosnia and Herzegovina is over half a *billion* Euros¹²⁶. This is mainly caused by the creation of 'ghost companies', an estimated 20,000 of which existed in Bosnia in 2004, that have used the old customs and retail taxation systems, as well as lack of synchronization of the tax systems between entities to avoid paying taxes. In the words of Paddy Ashdown, who in February of 2003 issued a Decision establishing an Indirect Tax Policy Commission tasked with introducing a single customs administration and a single State-wide VAT system in BiH, the current system had, in effect, “turned customs and sales tax into factories for fraud¹²⁷”. These ghost companies abused the taxation system, and avoided paying the final sales tax on imported goods by either claiming that the goods were sold to another retailer in the other entity from the one they were registered in, or simply by selling the goods on the black market. Aside from the direct loss of sales tax revenue for the government, these practices have flooded the Bosnian market with imported goods that are cheaper than the domestic ones, thus further hurting the domestic economy¹²⁸. The creation of a unified, state-level VAT system closed that tax loophole by charging VAT on imports directly at the border, and created strong incentives for full trade and revenue reporting by companies, as it became in their interest to receive refunds on VAT paid in the intermediate process of production. Both of these effects are anticipated to strongly lower the amount of gray activity.

¹²⁵ OHR, February 12, 2003. “High Representative Establishes Indirect Tax Policy Commission”

¹²⁶ IMF, 2005. Pp. 75.

¹²⁷ OHR, February 12, 2003. “High Representative Establishes Indirect Tax Policy Commission”

¹²⁸ Alic, 2003.

The political reasons for a state-wide VAT systems are no less compelling than the economic ones. Accession to the European Union, a future supported by a strong majority of Bosnia's citizens, is conditioned on there being a strong enough central government to be able to fulfill the tasks, and meet the challenges of accession. The EU, as well as other international actors such as the World Bank, and IMF, seek a single, unitary counterpart with whom they will be able to negotiate terms of membership, development loans, monetary and fiscal policies of Bosnia, and its unified economic space. Due mostly to these demands, as well as pressures and initiatives of the international community, the central government, envisioned as having a very limited mandate under Dayton, developed significantly, both in terms of its competencies, and state institutions. From a mere 3 Ministries established in 1995, number of state institutions grew from 17 in 2000, to 40 in 2004¹²⁹. With the growth in state competencies, and institutions needed to fulfill new tasks, the cost of central government has also increased significantly over the years.

Dayton, along with providing the central government with next to no operational duties, also left it with no independent source of funding. Until the creation of the ITA, and implementation of the Single Account in 2005, the state depended on monthly cash-transfers from the Entities. The amount of total annual transfers to the state was left at the discretion of the Entities, and they have resisted increasing that amount despite increased costs of running an enlarged central government. As a remedy for this system of state funding, ITA was created through the implementation of Indirect Tax System Law in 2003, and eventually Entity customs administrations were placed under the authority of the new agency. On January 1, 2005, the 'single account' became operational. Under the new state-level indirect taxation system, all revenues gained through indirect taxation (import and export taxes, excise duties, as well as sales taxes on goods and services) pool in the single account. From there, ITA automatically transfers funds to the state for the purpose of covering its administrative and debt

¹²⁹ IMF, 2005. Pp. 88. Number includes both the Ministries, and other institutions operating on the state level, such as the Indirect Taxation Authority, Public Broadcasting System, etc.

servicing obligations, and the rest is redistributed back to the entities and the Brcko District. After the implementation of the VAT system that replaced the sales taxes in both Entities, the VAT revenues also started being collected in the single account. The new system, aside from streamlining the collection process and fulfilling EU's requirements, was also seen as much needed solution for the problem of increasing public expenditure. The expected increase in overall revenues following the state-wide implementation of VAT would help cover the high costs of the government – the budgetary needs of the Bosnian government and its institutions are around 150 million Euros, but close to 10 times that amount would be needed to ensure effective functioning¹³⁰. These arguments add up to a strong case for implementing a state-wide indirect taxation system, both in terms of economic and political development, but there has still been a strong level of opposition to its implementation.

Arguments against VAT

Unsurprisingly, given the level of political and institutional fragmentation in Bosnia, there has been strong political resistance against the implementation of a state-wide indirect taxation system. As a creation of any state institution in effect means an increase in centralization of Bosnia, bringing with it a transfer of competencies from the entity to state level, such moves are usually vehemently opposed by lower levels of government, be it on cantonal or entity level. This is especially the case with Republika Srpska, where the sentiment towards Dayton has evolved from the outright rejection of its basic tenets during the immediate post-war period, existence of Bosnia as a nominally unitary country being but one of them, to strong support for its strict interpretation and application, as it is seen as guaranteeing the continued existence of a strongly autonomous Republika Srpska. Given this, transfer of competencies from the entity to state level has been an uphill process, strongly pushed for by the international actors and Bosniac politicians, and strongly resisted by the Republika Srpska's politicians.

¹³⁰ Skrbic, 2004.

The sentiment towards creating a state-level indirect taxation authority could only have been even more hostile, as it involved not just transfer of competencies from Republika Srpska to the state, but also because it involved transfer of control over collection and redistribution of revenue. Under Dayton, the entities were obligated to “provide all necessary assistance to the government of Bosnia and Herzegovina in order to enable it to honor the international obligations of Bosnia and Herzegovina¹³¹,” and the central government was financed by the Federation and Republika Srpska, where two-thirds of the annual budget, adopted by the Parliamentary Assembly, came from the Federation, and one-third from Republika Srpska¹³². As previously mentioned, this process of funds transfers was often politicized and delayed, and the entities had full discretion when setting and implementing their tax policies, including revenue collection. To agree to a unified customs and indirect taxation system meant to give up a significant amount of autonomy, and of a very sensitive kind – that of control over revenue collection.

The reaction from Republika Srpska to the proposal was in the beginning, unsurprisingly, very negative. It was described as a “hit on financial sovereignty and economic integrity of Republika Srpska,¹³³” and as a tactic that would rob RS of its tax revenue. The initiative to create a unified, centrally-governed taxation system in Bosnia was championed by the international community from as early as 2000, but in 2002 the international economic organizations in Bosnia, namely the IMF and the World Bank, started pushing for a unified VAT system. After a year of no progress, the US and EU clamped down on Entity governments. European Commission's Representative for Foreign Relations, Chris Patten, sent a strongly-worded letter to the Entities on January 21, 2003, threatening with sanctions if an agreement about the common VAT system was not reached by February 19: “The EC and all other international organizations will cease all donations and assistance to Bosnia. If Bosnia wants to join the European Union, it must have a VAT on a state level. There are no negotiations about

¹³¹ Constitution of Bosnia and Herzegovina, Art. III.2(b).

¹³² Constitution of Bosnia and Herzegovina, Art. VIII.

¹³³ Patriot Magazine, March 2004.

that.¹³⁴ In concrete terms, this mean that no further macro-financial assistance, 60 million Euros worth, would be forthcoming until the agreement was reached¹³⁵. The US government, on the other hand, warned that membership to the World Trade Organization is directly tied to the implementation of the VAT system. Following that, High Representative Paddy Ashdown still had to issue a decision a week before the February deadline by which he established an Indirect Tax Policy Commission, tasked with working out “how revenue will be allocated, how the administration will be structured, how it will be supervised by the Entities and the state, and how it will be audited.”¹³⁶ The Commission consisted of seven members – two from each Entity, two from state, and a chairman chosen by the European Commission, a Senior European Commission official Jolly Dixon.

The High Representative tried to explicitly assure Republika Srpska that the tax system reforms were not about undermining Republika Srpska, or about centralizing Bosnia, but about ensuring efficiency and preventing tax fraud: “The principles for the introduction of these reforms that I have established today *guarantee* that the Entities will receive at least as much revenue as they receive from the current system.”¹³⁷ As an effort to further mollify RS leadership, the center of the ITA was located in Banja Luka, and its Governing Board, created under the Law on Indirect Taxation System in Bosnia and Herzegovina, makes decisions based on consensus of its members. The Governing Board is responsible for “determining proposals for indirect tax policy, it defines strategic goals and approves the ITA annual plans of operation, ITA budget, bylaws and other implementing regulations prepared by the ITA”, and its seven members consist of the Chairman, three Finance Ministers (Minister of Finance and Treasury of Bosnia and Herzegovina, and the Finance Ministers of the two Entities), three indirect tax experts (one appointed by each Entity, and one by the state government), and three observers with no right of vote (Director of ITA, and an observer from Brcko District and from the Central Bank of

¹³⁴ Alic, 2003.

¹³⁵ OHR Press Release, February 3, 2003.

¹³⁶ OHR Press Release, February 12, 2003.

¹³⁷ Ibid.

Bosnia and Herzegovina)¹³⁸. If consensus cannot be reached, decisions are reached in the following manner:

* In matters relating to the introduction of import and export duties and any changes in such duties, a majority of GB members' votes are required, including the vote of the Minister of Finance and Treasury of Bosnia and Herzegovina.

* In matters relating to other indirect taxes, including the rates and structures of such taxes, the simple majority of GB members' votes is required, including those of the Republic of Srpska and Federation Finance Ministers. This voting procedure also applies to any decision in relation to any exemption from or amendments to indirect tax rates and structure.

* In matters relating to the allocation of the indirect tax revenue, a simple majority of GB members' votes is required, including the votes of all three Finance Ministers.¹³⁹

Effectively, this means that no decisions relating to the allocation of revenue, or changes in the rates and structure of indirect taxes can be made without the consent of the Entities, giving them a de facto power of veto on all important decisions. Though the Law on Indirect Taxation System in Bosnia and Herzegovina was passed at the end of 2003 by the Parliament, and not imposed by the High Representative, it is clear that this achievement, and the groundwork it laid for the establishment of a single VAT system in Bosnia, would not have been achieved without the intense pressure of the international community.

The Legislative Process

What, then, can we glean from the process of establishing a unified VAT system in Bosnia?

Hailed as a one of the most important laws since Dayton, one that will be instrumental to bringing

¹³⁸ Law on Indirect Taxation System in Bosnia and Herzegovina, Art. III.16-18, and Art. VI.28-29.

¹³⁹ Law on Indirect Taxation System in Bosnia and Herzegovina, Art. III.19.

Bosnia within the fold of Europe, and one that was a product of local workmanship and compromise, VAT was widely touted as a major success on the road to reintegrating Bosnia. Whereas Ashdown imposed the necessary first steps by creating the Indirect Taxation Commission in February of 2003, indicating that the international community would play a strong role in ensuring that the restructuring of Bosnia's tax system was done in a timely manner, he judged further steps taken towards the establishment of a single indirect tax system in Bosnia as being reached through domestic compromise¹⁴⁰.

To say that the indirect taxation system was reformed based solely on the reformist initiative and willing consensus of Bosnia's politicians would be, to put it mildly, an exaggeration. On the other hand, HR Ashdown did not have to employ the Bonn powers in order to ensure the eventual implementation of the VAT law – though the process, in total, did take nearly five years, it was brought about by following established democratic procedures in effect in a constitutional democracy. Once established, the Indirect Taxation Authority acted within its mandate, and created a proposal for the VAT law, then sent it to the Council of Ministers. This executive body then sent the proposal to the two houses of parliament, which debated the proposal, proposed amendments to it, agreed on a synchronized version of the text, and voted to adopt that text as a Law on Value Added Tax. With its implementation on January 1, 2006 Bosnia came one step closer to becoming a self-sustainable state firmly sent on the road to European integration. Or so the official story goes.

Through analysis of transcripts of parliamentary discussions in the two houses of Parliament on the implementation of the VAT Law, a different picture emerges. We are shown Bosnia's politicians fully aware of strong international intervention into the decision-making process, but unable or unwilling to act in opposition to it. A Dayton-esque outline of a new indirect taxation system emerges, one supposedly created to avoid inefficiencies caused by the decentralized Dayton system. An old era system of governance is revealed, one of the 'passive government', full of grandiose rhetoric and empty

¹⁴⁰ Ashdown's speech to the Venice Commission, 2004. Pp. 17.

of decisions based on analysis and void of accountability, with nationalist politicians beholden to their party bosses and solely focused on securing their positions.

Analysis

What does the process surrounding this important structural law, described in turns as “more than important”, as one of the “most important laws ever to cross parliamentary desks”, a “key law” bringing Bosnia closer to European integration, and helping create a single economic space within Bosnian borders, tell us about the level of self-sustainability of the democratization process in Bosnia? Previously I have pointed out three factors that have a negative impact on the development of an independent, local process of democratization in the country: decentralized, complex institutional set-up of the country and its system of governance as enshrined in the Dayton accords; the dependency and lack of accountability of the local decision-makers due to the strong use of executive powers by the Office of the High Representative; and the continued culture of the socialist-era rule by the cult of the 'expert' with no reliance on strong data analysis of the issue or consultation with affected interest groups and society at large, where the focus is on preserving power, not implementing measures conducive to long-term development.

Analysis of the parliamentary discussions held on the topic of VAT law have confirmed that all three factors have strongly impacted and to a great deal shaped the legislative process. This was a law deserving of “Made in Bosnia and Herzegovina” stamp not because it was made independent of international interference – it was very much guided by it – but because it clearly reflected truly Bosnian dynamics: Dayton's ethno-institutional fragmentation, and self-serving inertia, bordering on outright incompetence, of nationalist politicians.

Contextual Factors

The proposed text of the law was sent to the Parliament by the Council of Ministers (CoM) at the end of July of 2004. At that time, following the 2002 elections, the ruling coalition in Bosnia and Herzegovina was comprised of politicians from the three main war-time parties, SDA, SDS and HDZ. Seats of the three-member Presidency were filled by politicians from those three parties. The Chairman of the Council of Ministers (a role somewhat akin to that of a Prime Minister) was Adnan Terzic, an SDA member. Minister of Finance and Treasury was Ljerka Maric, HDZ.

In the Parliamentary Assembly, with its two chambers, the House of Peoples and the House of Representatives, the situation was similar. The House of Peoples consists of 15 members, who are chosen by the parliaments of the entities, and according to the ethnic key – five Bosniacs, five Croats, and five Serbs. The House of Representatives consists of 42 members who are directly elected by the voters of the entities, with two-thirds elected from the territory of the Federation, one-third from the territory of the Republika Srpska. No law can enter into effect without being approved by both chambers. The caucuses in the House of Peoples are based on ethnicity, and that chamber is seen as tasked with preserving the interests of the nations, whereas in the lower chamber the caucus determinant is political party membership¹⁴¹.

At the time of parliamentary discussions on the VAT law, the three ruling parties held 20 out of 42 seats in the lower house, and 12 out of 15 seats in the upper house of the Parliament¹⁴². The main opposition parties, the Socialdemocrats (SDP), Party for BiH (SBiH), both from Federation, and SNSD from Republika Srpska, held between them 13 votes in the House of Representatives, and only SDP had a member in the House of Peoples. This would indicate that the ruling coalition of the three nationalist parties would, if coordinated, have no problems in passing legislation they support through the upper house of the parliament.

¹⁴¹ Constitution of Bosnia and Herzegovina, Article IV.

¹⁴² Source: National Elections Commission for Bosnia and Herzegovina. www.izbori.ba.

Legislative Process in the Parliamentary Assembly

The text of the law sent to the parliament by the CoM called for a single VAT rate set at 17%, and a limited number of goods and services which were exempt from VAT. That text of the law is in general agreement with the Sixth EU VAT directive¹⁴³. The law itself was drafted by the Governing Board of the ITA, in consultations with outside experts, mainly European Commission's Customs and Financial Assistance Office (CAFAO), the IMF, and staff from the OHR¹⁴⁴. The Council of Ministers then put their stamp of approval on ITA's draft, and sent it to the Parliamentary Assembly for a vote. Upon the receipt of the proposed law, the Finance and Budgetary Commission of the House of Representatives reviewed the text and, taking into account amendments filed by the members of the House of Representatives, drafted its proposal for changes to the law, suggesting instead the offered single rate set at 17% that the VAT law install three differentiated rates – a 0% rate on certain goods such as bread, baby food, newspapers, textbooks; a reduced rate on agricultural products and services among other things, and a standard VAT rate to be applied to all other goods and services¹⁴⁵. One of the amendments discussed was that filed by Zlatko Lagumdžija, president of the Socialdemocratic Party (SD), which called for rates of 0, 8, and 18%, respectively. Though the actual rates were not determined at that time by the parliament, by changing the basic principles of the proposed law, namely the call for three differentiated rates, the Finance and Budgetary Commission, through its recommendation, effectively rejected the original text of the law as proposed by the Council of Ministers.

Present at the session on September 8, 2004, were Minister of Human Rights and Refugees,

¹⁴³ Per the Directive, the standard VAT rate must be at least 15%, while one or two reduced rates with the minimum rate of 5% can be authorized for “supplies of goods or of services having a social or cultural purpose”.

¹⁴⁴ Deputy Minister Kumalic, in his address to the House of Representatives on September 8, 2004.

¹⁴⁵ As noted by a number of parliament members, the law current at the time had taxation rates set at 0% for milk, bread, and medicine among other things, 10% on agricultural products and services, and food, and 20% for everything else.

Mirsad Kebo, and Deputy Minister of Finance and Treasury, Jusuf Kumalic, with no representatives from the ITA¹⁴⁶. During the course of the discussion in the House of Representatives, Deputy Minister Kumalic addressed the parliament, as a representative of the Council of Ministers, and effectively supported the Commission's recommendation that would create three differentiated VAT rates, saying that the original recommendation from the General Board of ITA to the Council of Ministers called for three rates – a rate of 0%, a reduced rate of 10%, and a standard rate of 20%¹⁴⁷. According to Deputy Minister Kumalic the current text of the law calling for a single rate of 17% was drafted only after consultation with, and insistence of the European Commission, and the IMF. Kumalic further went on to say that the proposed rate of 17% would ensure coverage of the current fiscal position, in terms of revenue collection, as achieved by the existing 0, 10, 20% system, ensure a more stable indirect taxation system, and was within logistical (personnel, equipment, knowledge) limits of what the ITA can implement at the time. However, he went on to point out that 23 out of 25 EU countries have the standard rate, and one or two other reduced VAT rates, and that a single 17% VAT rate in Bosnia would increase prices of basic foodstuffs.

A number of parliamentarians took note of the fact that, for a law of such singular importance, the Council of Ministers, nor the Governing Board of the ITA, which recommended the single rate to the CoM, did not send any representatives able to discuss and expand on their proposition aside from the Deputy Finance and Treasury Minister. Lack of respect for the parliament by the executive body, lack of any qualitative support for the proposed single VAT rate of 17%, and general lack of calculable data that could be used for comparison between different VAT rates and their effect on revenue were brought up as points of discontent by a large number of the members participating in the discussion, including members of PDP, SNSD, SDS, SDP, HDZ and SBiH – both members of the opposition, and

¹⁴⁶ Unofficial minutes of the 43rd Session of the House of Representatives; Parliamentary Assembly of Bosnia and Herzegovina, No. 01-50-1-15-43/04.

¹⁴⁷ Kumalic, unauthorized transcript of the 43. session of the House of Representatives held on September 8, 2004. An interview with the Deputy High Representative Donald Hays as late as August 17, 2004, seems to indicate that even at that time the VAT law predicted for two rates – a 0% rate, and a standard rate of 17%. Available at www.ohr.int

ruling parties. After a long discussion, out of the members present and voting, 33 voted for, 0 votes against, and 2 abstained, the House of Representatives passed the motion accepting the proposition of the Budgetary and Finance Commission which recommends three differentiated VAT rates, and calls for an additional 15-day amendment and analysis period during which the actual VAT rates should be determined, and new amendments could be submitted and presented to the parliament.

The parliamentary discussion on the law in the House of Peoples was held a day later, on September 9. The members of the House of Peoples took into account the resolutions brought by the lower house the day before, and the recommendations of its own Financial Commission and amendments to the proposed law by their members, which also called for differentiated VAT rates, but with the rates of 0, 10, and 20 %, respectively. In the words of Mustafa Pamuk (SDA), noted that the Commission of the House of Peoples considers the mentioned rates to be the best solution, while the House of the Representatives voted for the rates of 0, 8, and 18% VAT rates. He went on to say, “Therefore, we agree on one thing – we need differentiated VAT rates.¹⁴⁸” Osman Brka (SDA) concurred, saying that he “was convinced that the suggested rates and amendments that are adopted by the Commission are today the best solution for BiH, which does not mean that they will be the best solution in a year or two, but today it is definitely so.¹⁴⁹”

It was suggested by a number of representatives that the discussions and resolutions brought by the House of Representatives were influenced by the upcoming local elections to be held in October. The representatives also noted, in a reprise of the sentiment expressed in the House of Representatives, that there is no objection to the rationale and the need for a VAT law to be implemented, but that the difference in opinions is based on the number of rates to be implemented, and the social effect higher rates could have on the large number of unemployed, and financially vulnerable people in Bosnia. Given that, the House of Peoples also voted for a resolution accepting the recommendations of the

¹⁴⁸ Pamuk, Mustafa. Unauthorized transcript of the 28. session of the House of Peoples held on September 9, 2004.

¹⁴⁹ Brka, Osman. Unauthorized transcript of the 28. session of the House of Peoples held on September 9, 2004.

Finance Commission, calling for differentiated VAT rates, and instructed the Commission to report back to the parliament within 15 days with a new report on the proposed law, taking into account the discussion, and any further amendments brought before it. Out of the members present and voting, 11 representatives voted for, 3 voted against, with no abstentions.

In summary, one month before the local elections were to be held across Bosnia, representatives of both houses of the parliament overwhelmingly voted to reject the draft of the law presented by the CoM and ITA, instead calling for differentiated rates which would tax certain basic goods and services at lower rates, in deference to the difficult socio-economic situation faced by the majority of Bosnia's citizens. The Finance and Budgetary Commissions of both houses of the parliament were given a 15-day period to draft another proposal on the law, taking into account parliamentary discussions, resolutions for differentiated rates, and any new amendments submitted by the representatives. The fact that, out of the total of 49 representatives voting in both houses of parliament only 5 voted against these suggestions, as a sign of support of the original draft of the law and the single rate of 17%, shows that the proposal for differentiated rates had strong both with the representatives of the parties in power, and those of opposition parties.

The second reading of the proposed VAT law was held in the House of Representatives on November 4, 2004, one month after the local elections, and two months after the first VAT discussion. The Finance and Budgetary Commission had sent a new report on the proposed VAT law on October 27, nearly a month after the expiration of the 15-day deadline given to it by the Parliament. Unlike during the last discussion on the VAT law, present at the second reading were the Chairman of Council of Ministers, Adnan Terzic, Minister of Finance and Treasury, Ljerka Maric, as well as her deputy, Jusuf Kumalic. Present were also the Chairman of the Indirect Taxation Authority, Jolly Dixon, as well as a representative from IMF, John Novregaand.

The new report by the Commission, as discussed by the parliamentarians, did not employ the principles voted on in the last session, namely that agreement reached called for three differentiated

VAT rates, with actual rates to be determined. The Commission's new report called for two differentiated VAT rates, the 0% on medicine, bread, milk, etc, and a standard rate of 17% on all other goods and services.

Chairman of CoM Terzic addressed the representatives, arguing for a single VAT rate, and citing the need for efficient and quick implementation of the VAT law. Given that need, he went on to argue that ITA is not capable, with its current operational capabilities, of handling implementation of differentiated rates. He noted the fact that the law being discussed was the first law in the post-Dayton era where not invoking interests of Bosniacs, Serbs, or Croats, but is argued from the sides of ruling parties and opposition. However, he went to point out that the law on the System of Indirect Taxation that established the Indirect Taxation Authority, named that institution as the only body in Bosnia authorized to determine indirect tax policy, including tax rates. Thus, if the parliament passes a law that establishes taxation rates different than the ones approved by the Governing Board of ITA, that law will not be valid, as ITA has to give its approval to any indirect taxation policies.

The parliamentary discussion in a large part followed the argumentations brought forth in the past session; a large number of parliamentarians criticized the CoM for lack of any economic and statistical data and calculations as to the actual impact of different rates of VAT that had been proposed, both on the revenue collection, and on the effect it would have on consumers. It was notable that the strong criticisms also directed towards the Financial and Budgetary Commission for the changes made to the original parliamentary proposal that predicted three VAT rates, was split along the lines of opposition vs. ruling parties. Suggestions have been voiced by opposition parliamentarians that the cause for the switch in the Commission's report from recommending three rates, to supporting a 0% and a 17% rate was due to pressure and intervention by the members of the international community.

In the end, after the representatives voted down a number of amendments proposed by SDP that sought to ensure 0% taxation rate on a number of goods and services that were not taxed under the

previous system, newspapers, baby food and medical prosthetics among them, members of SDP walked out of the chamber before the vote was cast. After the voting, with 17 votes for, 10 votes against, and 8 abstentions, the VAT law with differentiated rates set at 0, and 17%, was passed by the House of the Representatives.

The next day, following the conclusions brought by the House of Representatives, Chairman Terzic sent his resignation to the Presidency of BiH. As an explanation he offered that he cannot support a law with two rates which would enable continuation of gray economy in Bosnia. He also noted that he failed to understand how it is possible that four heads of ruling parties have seats on the Council of Ministers, and yet the representatives of those parties in the parliament vote against the law sent there by the Council¹⁵⁰. As the acceptance of Mr. Terzic's resignation would have meant the fall of the government, the Presidency promptly rejected his offer of resignation.

The House of Peoples met for the second reading of the VAT law on December 14, more than a month after Mr. Terzic's offer of resignation. Chairman Terzic was there to address the parliament, and during his talk he said that a number of quantitative analyses on the single VAT of 17% were performed and shared with, and supported by, Entity Prime Ministers. In the course of his exposition, he said that differentiated VAT rates, as the ones voted on by the House of Representatives, serve the richer portion of the populace better as they spend more, that there is a strong need to implement VAT as soon as possible, and that a differentiated rate would make the process more complicated, and that a differentiated rate would enable continued gray economy. He did indicate that he is ready to work with the two entity Prime Ministers to work on a plan for programs of social protection for the most endangered portion of the population, set to take effect together with the implementation of the VAT law.

The Financial Commission of the House of Peoples then brought forth its recommendation, which stated that the version of the VAT law, as presented by the Council of Ministers, with a single

¹⁵⁰ Kristo, November 2006.

rate of 17% should be implemented. As a reminder, the Commission initially, in September, found it necessary to change the basic principles of the law as drafted by the CoM, by recommending three rates – a 0, 10, and 20% rate, which was accepted by a strong majority of the House of Peoples members. The change in opinion was explained as a realization that the public, and the Commission presumably, was misled by claims that a single rate of 17% would be harmful, and that multiple rates would be more beneficial. No further analysis or data was given.

A number of representatives took the opportunity during the discussion to blame the House of Representatives for overly politicizing the issue, both in the media and the chamber. A few, including Chairman Terzic, took pains to refute the claims that the 180-degree U-turn the representatives of the House of Peoples had on the basic propositions of the law were due to pressure by international community. An SDA member criticized the CoM for failing to properly address and educate public on the issue, instead allowing the 'fog sellers' in the opposition to dominate the airwaves. The House of Peoples voted to pass the text of the law as it was proposed in the original by the Council of Ministers, attaching to it a number of resolutions, one of which called for the CoM to organize needed informational sessions for the public, citizens, private and public sector on the aspects of implementation of VAT law. The House of Peoples made no such resolution for the need for implementation of social protection programs. The law, along with the attached resolutions, passed with a vote of 12 for, and 1 abstention. As the law was passed in a form differing from the one accepted by the House of Representatives, a Commission was formed that would work with the Commission from the lower chamber on the synchronization of the two texts, and agreement on the final text of the law. One member each from SDA, SDS and HDZ was chosen as a member of the Commission.

Finally, on January 12, 2005, the House of Representatives met to vote on the synchronized text of the law as proposed by the agreement between the Commissions of the two chambers. Members of the Commission from the House of Representatives were from SDA, HDZ, and PDP RS (Party of

Democratic Progress from RS). That Commission, along with the Commission from the upper chamber of the parliament, agreed on the version of the VAT law with one standard VAT rate of 17%, and no 0%, in effect accepting the original draft of the law proposed by the CoM in September.

A number of parliamentarians from opposition parties took to the podium to denounce what they saw as a 'sell out' of the integrity of the House of Representatives by the Commission. A member from RS noted that the outcome of Commission's activity should have been obvious to everyone once members of the Commission were selected from the leading parties. An SDP representative denounced what he saw as a campaign of disinformation and pressure by the Council of Ministers, as they had presented a number of reports that showed the benefits of a single VAT rate to the Commission during its meeting. According to this member, those materials presented to the Commission, but not to the rest of the House of Representatives, were directly drafted by the international community and passed through the CoM onto the Commission, and are not factually correct. A member from SDS mentioned that the pressure exerted on the House of Peoples, as well as the parliamentarians of the lower chamber, was well known to everyone, and was most likely the cause for the Commission's report that agreed with the original proposal of the VAT law. Selim Beslagic of SDP mentioned an interview with the Deputy High Representative, Mr. Hays, done shortly after the House of Representatives had accepted a draft of the law that contained two VAT rates, a 0% and 17% rate. According to Beslagic, Deputy's response to the question as to what will happen with the law was to say that the House of Peoples would accept the law as proposed by the CoM, and after a Commission to agree on a common text of the law was formed, a law with a single rate would be passed. Beslagic pointed to the futility of spending four months debating the law in parliament, when the end result seems to be predetermined¹⁵¹.

The law was voted on, and passed with 19 votes for, 11 against, and 3 abstentions. Next session of the House of Peoples on the topic was held on January 26, where the law was accepted with no

¹⁵¹ Selim Beslagic, unauthorized transcript of the 50. session of the House of Representatives held on January 12, 2005.

discussion, with 10 votes for, and 1 against.

Main Findings

Two things become very obvious in the first reading of the parliamentary discussion transcripts. The first one is that the parliamentarians are discussing a law they consider to be 'fundamental' in its importance, instrumental for uniting Bosnia's economic space, and fighting criminal economic activity, but are not provided with the most basic economic data on which to make judgments as to the effects of implementation of one VAT rate vs. another, or given statistical analyses that would compare the impact of a single-rate system vs. a differentiated-rate system in Bosnia. There are two sides to this issue: on the one are the Council of Ministers and the Indirect Taxation Authority, as the creators of the law, and determinants for the single-rate VAT of 17%. On the other one are the two houses of the parliament, as the country's state-level legislators who are responsible to examine the merits and drawbacks of proposed laws, make amendments they see as necessary, demand necessary information to make informed decisions, and accept or reject laws based on conclusions drawn from parliamentary discussions, presentations by experts, and analysis of available information.

For a law that completely transformed the entire indirect taxation system of the country, and strongly affected the fiscal position of the economy, parliamentary discussions show a stunning lack of knowledge-based decisions. The law on instating a drastically different system of indirect taxation on a country-level was sent to the parliament by the Council of Ministers and the ITA without any quantitative back-up. Chairman Terzic has mentioned 'teams of experts' that provided 'detailed analytical calculations' that supported the creation of a single rate set at 17%, but neither the CoM, nor the ITA which gave the calculations to the CoM, ever presented those analyses to the parliamentarians. In the words of Ljiljana Milicevic (SDS), a member of the Financial and Budgetary Commission of the

House of the Representatives that brought the recommendation of instituting a differentiated VAT rate of 0, 8, and 18%, the Commission members were “left on their own” to make determinations as to the best rate of VAT¹⁵². Furthermore, per the statements made by the Finance and Treasury Deputy Minister Kumalic, the original calculations made by the local experts and the European Commission's Customs and Fiscal Assistance Office (CAFAO) supported a differentiated rate. It was not until the Chairman of the General Board of the ITA, Jolly Dixon, consulted IMF and the EC that a single standardized rate was insisted upon.

We can conclude two things out of this. One, the Council of Ministers is highly susceptible to 'suggestions' from the international community, and two, the CoM's interaction with the Parliamentary Assembly seems to mimic that of the international community's interaction with the CoM – namely, the much-criticized approach of OHR to Bosnia's law-makers where OHR drafts legislation and expects it to be implemented without much discussion, is now visible in the relations between Bosnia's executive and legislative branch. The Council of Ministers, if we are going to go by the Deputy Finance and Treasury Minister's statement, should have had two sets of calculations: one created by CAFAO and local experts, calling for a differentiated rate, and one created by IMF, calling for a single, 17% rate. If the IMF analysis showed that the single rate approach was better, there would have been no reason for the CoM not to release both sets of analyses to the Parliamentary Assembly. If, however, the single 17% rate was chosen because of EC and IMF's preference for it, not because of statistical analysis confirmed its superiority to other options, then the 'ownership' of the reforms process of Bosnia's executive branch becomes more suspect, and the 'autism'¹⁵³ of state-administration becomes more apparent.

Lack of will to share operational data with the parliament is another worrisome indicator. By withholding the basic information needed for the members of the parliament to be able to make

¹⁵² Milicevic, Ljiljana. Unauthorized transcript of the 43. session of the House of Representatives held on September 8, 2004.

¹⁵³ “Arithmetic of Irresponsibility”, June 2005. Pp. 5.

educated decisions on a law deemed extremely important by all members of the Parliamentary Assembly, the Council of Ministers seems to have little regard for the democratic process of law-making. Given the end-result, where amendments from both houses of the parliament calling for a differentiated rate were overruled by parliamentary commissions staffed with hand-picked nationalist politicians, it is hard not to question the authenticity of the parliamentary process. Halid Genjac (SDA) noted during his discussion in the House of Peoples that heads of three ruling coalition parties have seats on the Council of Ministers and that “they should be enough to convince their delegates, and ... get support for this law in the House of Representatives as well¹⁵⁴.” In the end, the will of the party won out over any factual discussion over different VAT rates, and party members in the parliament fell in line, passing the law in the original version.

The lack of any quantifiable data offered by the CoM and ITA did generate a large number of complaints by the members of the parliament. Sead Avdic, SDP member of the House of Representatives, early on in the discussion process asked for the presence of the work-group responsible for drafting of the law, representatives of the CoM and the General Board of ITA to be present during parliamentary discussions, in order to provide the parliamentarians with the needed explanations and information¹⁵⁵. In both houses members of opposition parties, but also of governing parties¹⁵⁶, demanded to be given more information on how the rate was calculated, and how it compares to calculations done for a differentiated rate. However, despite being given no information on the full fiscal and economic effects of the law both on the revenue or on the social situation in Bosnia, and admitting a general lack of knowledge of fiscal economics, and taxation instruments, the parliamentarians considered themselves well-equipped not only to discuss the merits and drawbacks of

¹⁵⁴ Halid Genjac, unauthorized transcript of the 34. session of the House of Peoples held on December 14, 2004.

¹⁵⁵ Sead Avdic, unauthorized transcript of the 43. session of the House of Representatives held on September 8, 2004.

¹⁵⁶ Such demands were made by members of opposition parties, such as Sead Avdic (SDP), Nikola Spiric (SNSD), and others, but also members of the parties of the ruling coalition, such as Ruza Sopta (HDZ), who sat on the Finance and Budgetary Commission of the House of Representatives, Momcilo Novakovic (SDS), and Fatima Leho (SDA). Unauthorized transcripts of the 34., 46., and 50. session of the House of Representatives.

the law in its proposed form, but also to make wide-reaching amendments to it¹⁵⁷. It was not until second reading in the House of the Representatives that the members of one party, SDP, brought forth the calculations on which they based their proposed amendments but at that time, after the resignation threat by CoM Chairman Terzic, the tide of support for 'socially-aware' amendments had turned.

Another notable thing is the level of international impact on the decision-making process. Unlike at other times when a law simply would not have been made were it not for pressure by OHR and other international actors, no parliamentarian questioned the need to bring a VAT. Not one member argued against the implementation of the VAT system – the divisions were not between those for, and against VAT, but between those arguing for a single rate, and those arguing for a differentiated rate. Given that Deputy High Representative Donald Hays was able to anticipate¹⁵⁸ a few months in advance exactly how the final machinations in the Parliamentary Assembly would work out, and that the single rate of 17% would be written into law, the strong role of OHR in the proceedings seems beyond doubt. If no strong analytical data was presented to support the single VAT rate of 17%, and the VAT law would have been passed in the Parliament, albeit with a differentiated rate, why was such notable behind-the-scenes work needed by OHR? In other words, if local 'ownership' of decision-making is the goal that would enable smooth phasing out of OHR's mission, OHR's intervention in a non-critical process¹⁵⁹ seems closer to the 'European Raj'¹⁶⁰ syndrome, than an operation dedicated to development of self-sustainable democracy.

Lastly, the Indirect Taxation Authority was created to unite the collection of revenue garnered

¹⁵⁷ Despite Sead Avdic's (SDP) call for some 'self-criticism', calling on the representatives to acknowledge that “we most likely do not have enough knowledge about such a complex law ... I don't think we have the right to allow ourselves the freedom to simply vote.” Unauthorized transcript of the 43. session of the House of Representatives held on September 8, 2004.

¹⁵⁸ This relates to the comment made by SDP member Selim Beslagic during the session of House of Representatives on January 12, 2005, described previously. The author was unable to locate the mentioned interview with Hayes for confirmation, but a number of other members of parliament have singled him out as the OHR's point-man campaigning for the single VAT rate of 17%.

¹⁵⁹ Out of, at that time, 25 member-states, 23 states in the EU were employing differentiated VAT rates, the solution sought by Bosnia's parliamentarians.

¹⁶⁰ See Knaus and Martin, 2003.

through indirect taxes and customs duties, to streamline the process, and ensure more efficient and less politicized redistribution of revenue, including the budgetary needs of state-level institutions. In practice, however, Dayton places taxation directly under the control of the Entities. In order to work around the constitutional restraints placed by Dayton, a compromise had to be made. ITA became a hybrid agency, effectively placed 'outside of the system'¹⁶¹ - it could not be placed under control of the central government, as that would be unconstitutional, but the idea was to get rid of three separate tax administrations. Thus, the Governing Board of ITA is the only body authorized to set indirect tax policy, and though it answers to the Council of Ministers, the Council of Ministers has no real authority over ITA. In effect, the warning Mr. Terzic sent to the parliamentarians as to the futility of arguing for a differentiated rate was correct – no such changes could, legally, be made without the approval of ITA. Bosnia's parliamentarians are not allowed to fully use their legislative powers on laws that stem with the ITA – any change has to be first approved by its Governing Board.

Though such a set-up could be seen as necessary in an effort to avoid the politicization of the process of revenue redistribution, the Governing Board of the ITA is composed of the Finance Ministers and “indirect tax experts” from both Entities, who have veto power. In truth, disputes over the redistribution coefficient of the revenues collected in ITA's single account started shortly after money started being collected in it. Entity disputes over who should get how much blocked the operation of the single account, paralyzing the redistribution of revenues¹⁶². Instead of a more effective central body, what ITA actually became under the constraints of the Dayton constitution is Bosnia's dysfunctional set-up writ small: a central governing board easily blocked by entity representatives veto rights and diverging interests and ideas.

¹⁶¹ Miljanovic, 2004.

¹⁶² See Miljanovic, 2006; OHR, May 4, 2007.

CONCLUSION

In the previous chapters I have talked about the challenges facing Bosnia as it seeks to emerge as a stable democracy with a self-sustainable economy. Three years of war have ravaged the country and left deep ethno-national divisions, and twelve years of concerted international efforts of state-building and democratization have not as of yet produced satisfying results. Three main factors were delineated as reasons for such lack of progress: the peace agreement that stopped the fighting and preserved the peace, the Dayton accord, is not a structurally and institutionally viable solution for developing a functioning state; ten years of international overlordship overseen by the Office of the High Representative achieved great advances in terms of state-level institution building, but has retarded the process of autochthonous democratization at best, and provided the local politicians with a technocratic, top-down example of ruling the country at worst; the local political elite, far from being truly divided by 'ancient hatreds', is operating on socialist-era nomenklatura mind-set, resistant to any change, focused on self-preservation, and lacking accountability.

The analysis of the process involved with the passage of the VAT law has shown that all three factors have had considerable effect on the legislative process, and the final result. The complex constitutional structure of Bosnia, as created under Dayton, has been cited as one of the main causes, if not the leading reason for its governance problems¹⁶³. The multiple levels of government, weakness of the state against the power of the Entities, and the paralyzing effects of Entity veto have all been listed as culprits leading to the lack of functionality and progress. Following this example, the Indirect Taxation Authority, an institution created to streamline and simplify a highly inefficient and costly system of indirect taxation that existed in Bosnia, ended up being crippled by the demands created by Dayton: As the constitution placed taxation under the control of the Entities, the ITA had to be created

¹⁶³ Venice Commission, March, 2005.

'outside the system', neither under the control of the Council of Ministers, and the Parliament, nor under the control of the Entity governments; its Governing Board, though a nominally independent body has been hobbled by the need to operate on consensus, and paralyzed by the veto power of Entity members. Even so, I would argue that Dayton, complex and burdensome as it is, would not present a serious stumbling block for the development of the country if there was a will by those involved to make it work. Internal structure of Bosnia, open to abuse and obstruction and easily paralyzed would, however, not prove a true break for advancement if the political will to make it work existed. Though the ITA, as created under Dayton restrains, proved to have a more cumbersome system of decision-making that would have otherwise been necessary, its continued paralysis is not a functional, but a political issue.

Which brings us to the two remaining factors, the effects of OHR's strong-handed approach to governing Bosnia, and the local political elite. In the past five years 'ownership' became the call word of international disengagement strategy in Bosnia. According to this theory, if the local politicians and populace could embrace the values and practices inherent in the concept of 'ownership' – in short, the responsibility for the future of their country, and the will to hold those in power accountable for their actions, or lack thereof – Bosnia's path to self-sustainability and European membership would be all but assured. Blind reliance on, and continued expectation of foreign political and economic aid, both by Bosnia's politicians and its citizenry, was seen as the main stumbling block holding the country back; if the nationalist politicians realized that the international community would not be there to slap their wrists over bad decisions, then hold their hands and lead them to the right ones, they will have to learn to cooperate and compromise with each other, and work together to find workable and lasting solutions for the political and economic logjam Bosnia finds itself in. Bosnia's electorate, on the other hand, would also be prodded into activity, and start making active demands out of their legislators, hold them accountable for the lack of results, and start voting for politicians who create jobs, as opposed for the ones who claim to be protectors of the threatened national interests.

In truth, what becomes obvious with analysis of the legislative process surrounding the VAT law, is that the OHR's practice of “do as I say, not as I do” may have worked in the short run, achieving and oftentimes simply imposing political compliance for the application of its policies, but has done next to nothing for developing leadership capacity and responsibility in Bosnia's political elite, or break their dependency on outside intervention. Following the example set by OHR's modus operandi over the years, and very much in the vein of 'party knows best' socialist governance, the Council of Ministers relied on the input and knowledge of a selected number of international experts to draft a crucial economic law, while putting in little to no effort to consult or engage local interest groups, or provide any amount of real analytical basis for the proposed changes to the legislative branch.

On the other hand, the politicians in the Parliament entrusted with debating the validity of the proposed law made no real effort to educate themselves on the matter, request numerical basis for the claims made by the Council of Ministers, nor engage in any substantial analysis of the subject, choosing to focus on empty pre-elections rhetoric that quickly gave way to the demands of their party heads once the time to cast votes came. A large number of legislators belonging to the ruling parties were content with taking for granted the “expert” opinions coming from the CoM as to the economic importance of adopting the single VAT rate. Those who then got up to the speakers podium to demand analytical accounting of the CoM's claims, and trumpeted the importance of alleviating the impact on the most endangered social layer of a generally impoverished citizenry, rolled over and voted with the party when the day of reckoning came. If we compare this performance with ESI's description of the socialist-era administrators, the similarities are striking:

“The socialist public administration was a “rule making elite”, relying on legislation which did not reflect real compromises among those it affected, and which as a result proved very difficult to implement whenever it clashed with real interests. Political rhetoric was shaped by the cult of the “expert” (strucnjak) – the technician who was thought to be best placed to determine the public interest. Political reality was characterised by the *passivity* of public institutions: reform debates replaced the daily work of building reform coalitions and generating popular support for the transformations which were needed.¹⁶⁴”

¹⁶⁴ ESI, 2004. Pp.3. Italics in the original.

If we add to this passivity of governance the fact that “Bosnian politics has a long tradition of tactically adjusting to the presence of external powers, and that those historical patterns of adaptation have been revived¹⁶⁵,” it is not surprising that the local politicians are relying on a top-down imposition of important policies without giving them much, if any, critical analysis. As we have seen from the parliamentary discussions on one of the most significant post-Dayton laws in Bosnia, “reform debates tend to be so superficial that policy makers have little need for reliable information.¹⁶⁶”

Indeed, it is the symbiosis between the demands and impositions placed by the consortium of the international players, with OHR at its helm, and the Bosnian political elite that is the most striking characteristic of the entire process surrounding the implementation of a VAT system in Bosnia. Far from fostering 'ownership' of the indirect taxation system reform process, the OHR, IMF, and the EC have supported the socialist-era passivity of the local politicians, and fed the governing bodies' “authoritarian temptation.” Defined as “a distrust of the democratic process, and a preference for a government of 'experts' who are isolated from the people they are supposed to serve,” authoritarian temptation is a legacy of the long-standing “tendency to look to outsiders to solve Bosnia's problems, rather than finding home-grown solutions¹⁶⁷.”

A stark confirmation of such an assessment can be find in the opinion expressed by a politician in the House of Representatives, responding to detailed, numerical arguments by a member of the opposition who called for differentiated VAT rates:

¹⁶⁵ Bose, 2002, in relation to the long history of foreign and/or top-down rule in Bosnia, including Austro-Hungary, the Yugoslav Monarchy, and finally the 50-year Communist rule. Pp. 269.

¹⁶⁶ ESI, 2004. Pp.5.

¹⁶⁷ ESI, 2004. Executive summary.

“I was present at a number of meetings organized about this law, and the World Bank, and the IMF, and the CAFAO, even the experts from OHR are advising us to accept the single rate at the moment when we are implementing VAT, on account of its efficient and functional implementation. Why should I, if I have no other calculations, be in the position to trust some private calculations that I hear today here in the Parliament and *not trust the calculations of the ones* [speaking of the above-mentioned international organizations] *who are, among other things, responsible to ensure the financial stability of this country.*¹⁶⁸”

After five years of verbal promotion of 'ownership' in Bosnia, starting with HR Petritsch, the analysis of the process surrounding the adoption of the VAT law shows us that the international community's activities belie their words. By simply trying to graft “a democratic nervous system onto an outdated totalitarian mental set-up¹⁶⁹,” and then continuing to support, through continued pressure and outright intervention, the passivity and dependence of the political elites they charge with taking on responsibility for bringing about democratization, the Office of the High Representative, and other international organizations operating in Bosnia, are in effect keeping the country on a short leash and making it trot in place, while continuously admonishing it for not running free. If the goal of the international community is to see the Bosnian political elite make the transition from being “subjects of an international mission,” and reach a level of democratic development where the 'authoritarian temptation' will be easy to resist, the analysis of the steps taken to draft, pass, and implement the 2005 Law on Value Added Tax shows us that both the local politicians and the international community are walking in the wrong direction.

¹⁶⁸ Sefik Dzaferovic, member of the SDA, and a representative at the House of Representatives, responding to Zlatko Lagumdžija's (SDP) detailed proposal for a list of amendments to the VAT law, including a differentiated rate. Unauthorized transcript of the 46. session of the House of Representatives held on November 4, 2004.

¹⁶⁹ Friedrich Ebert Foundation, 2005. Pp. 22.

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